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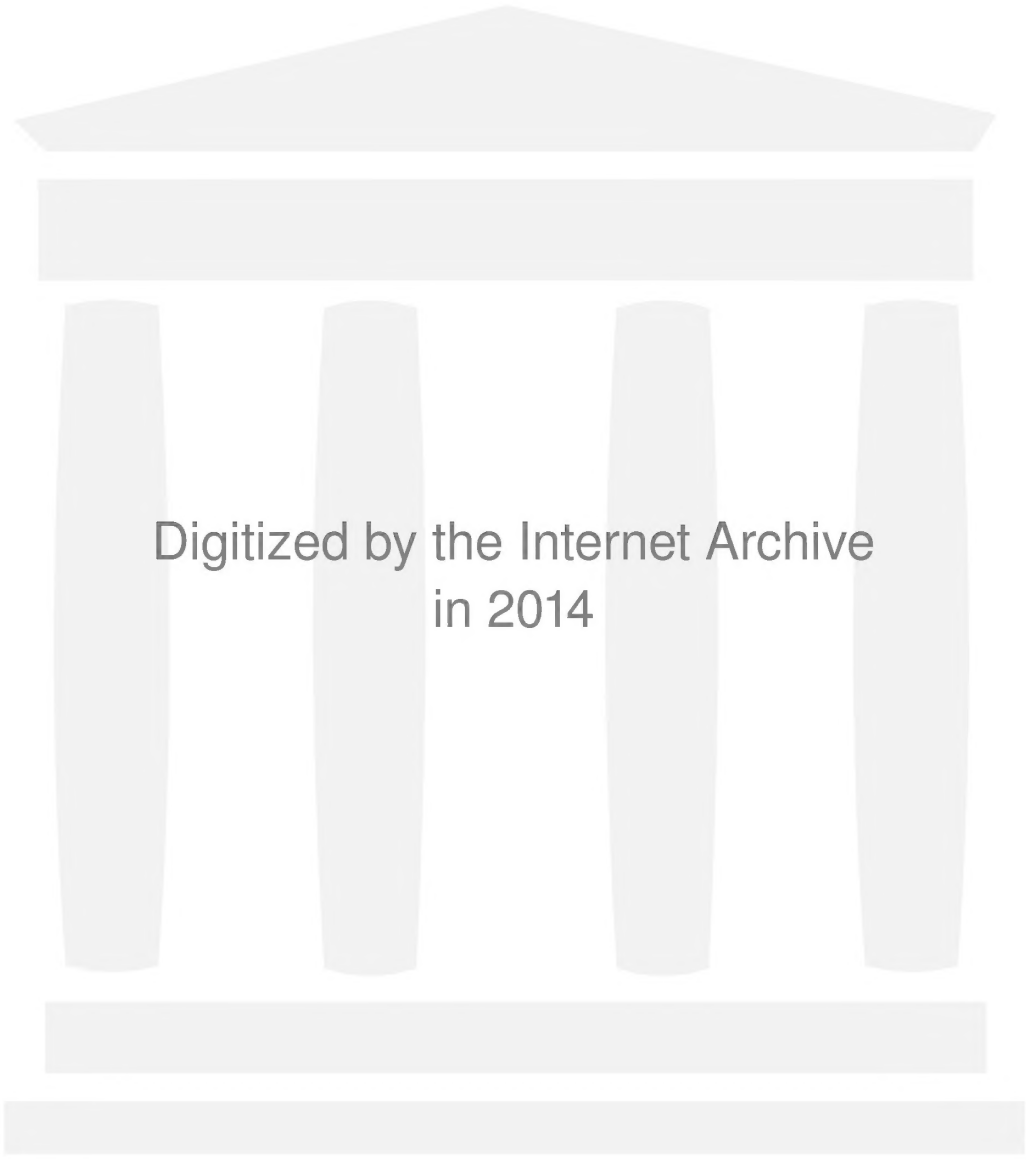
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January 8

...RICA'S KEY INDUSTRIES

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BusinessWeek

UARY 8, 1996 A PUBLICATION OF THE McGRAW-HILL COMPANIES $3.50

The 25 Top MANAGERS of the YEAR

PLUS: THE HOTTEST ENTREPRENEURS
THE BEST NEW PRODUCTS

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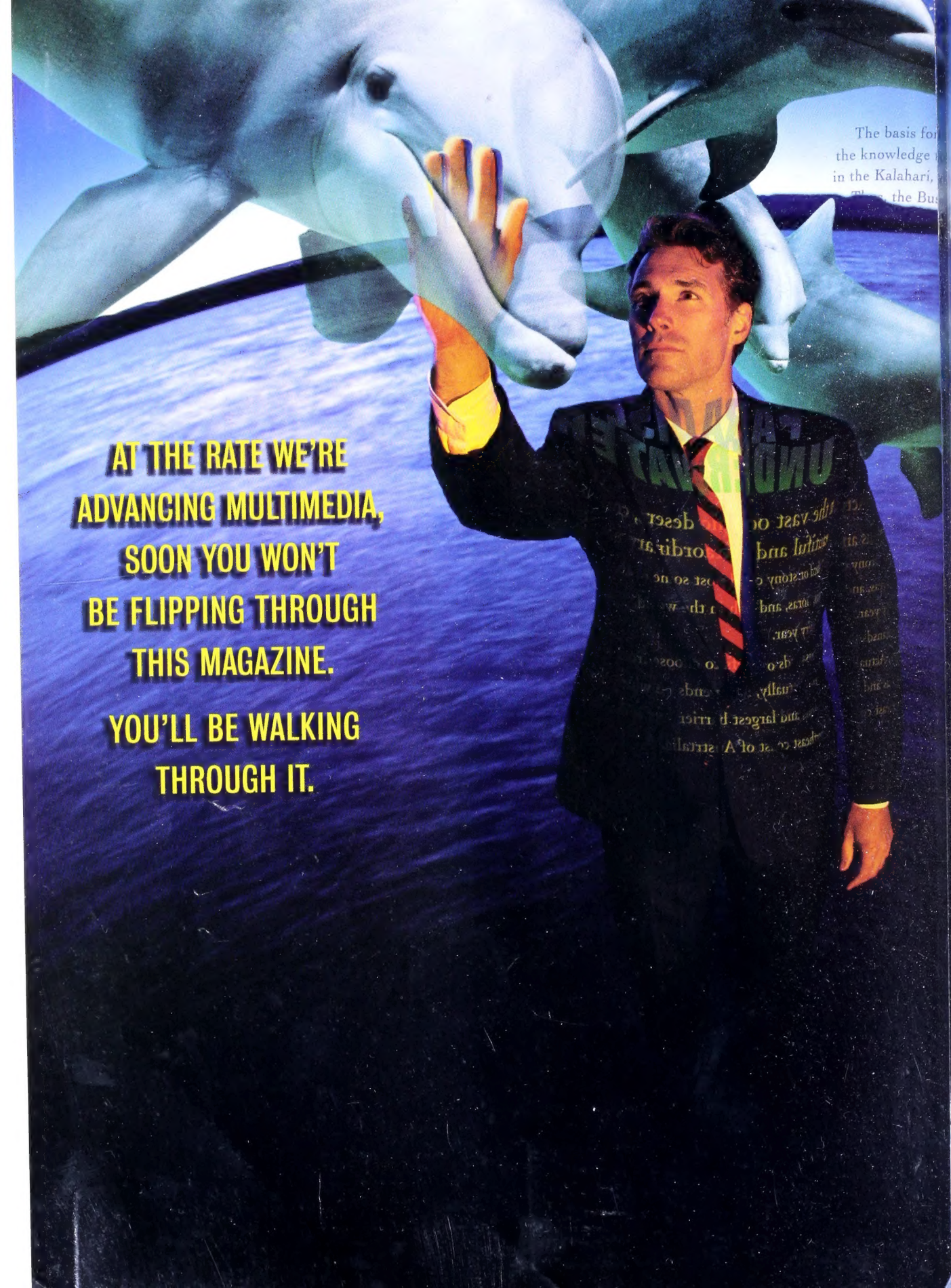
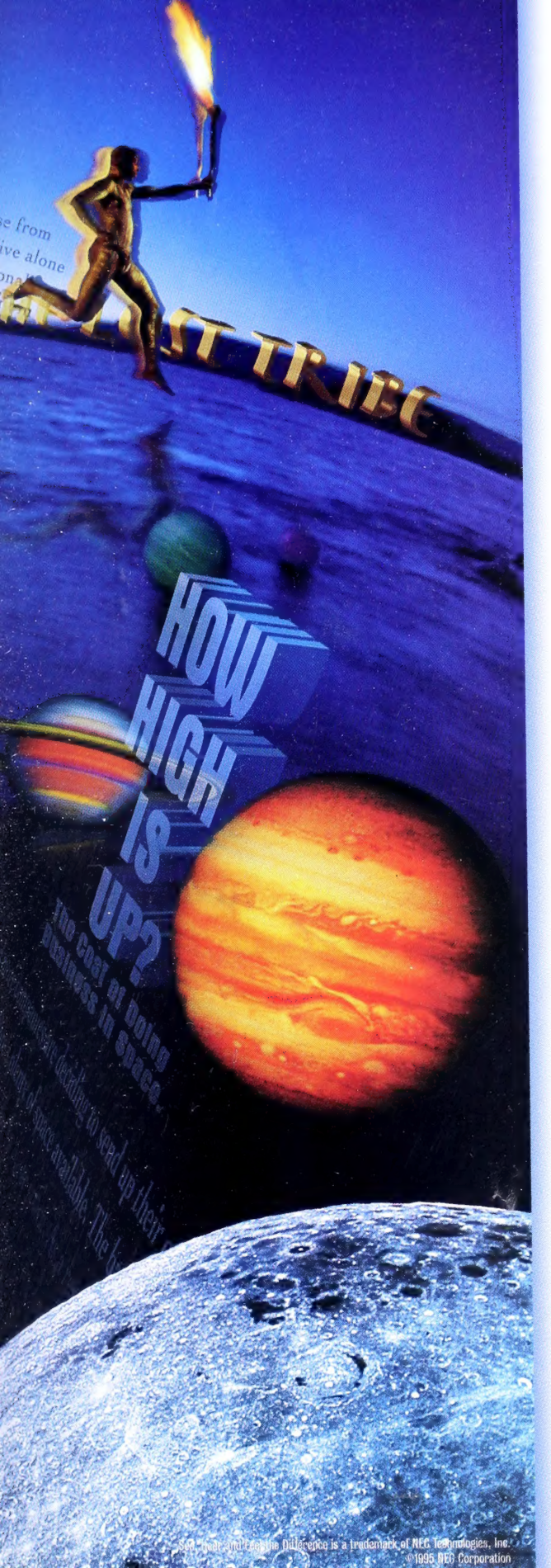

AT THE RATE WE'RE
ADVANCING MULTIMEDIA,
SOON YOU WON'T
BE FLIPPING THROUGH
THIS MAGAZINE.
YOU'LL BE WALKING
THROUGH IT.



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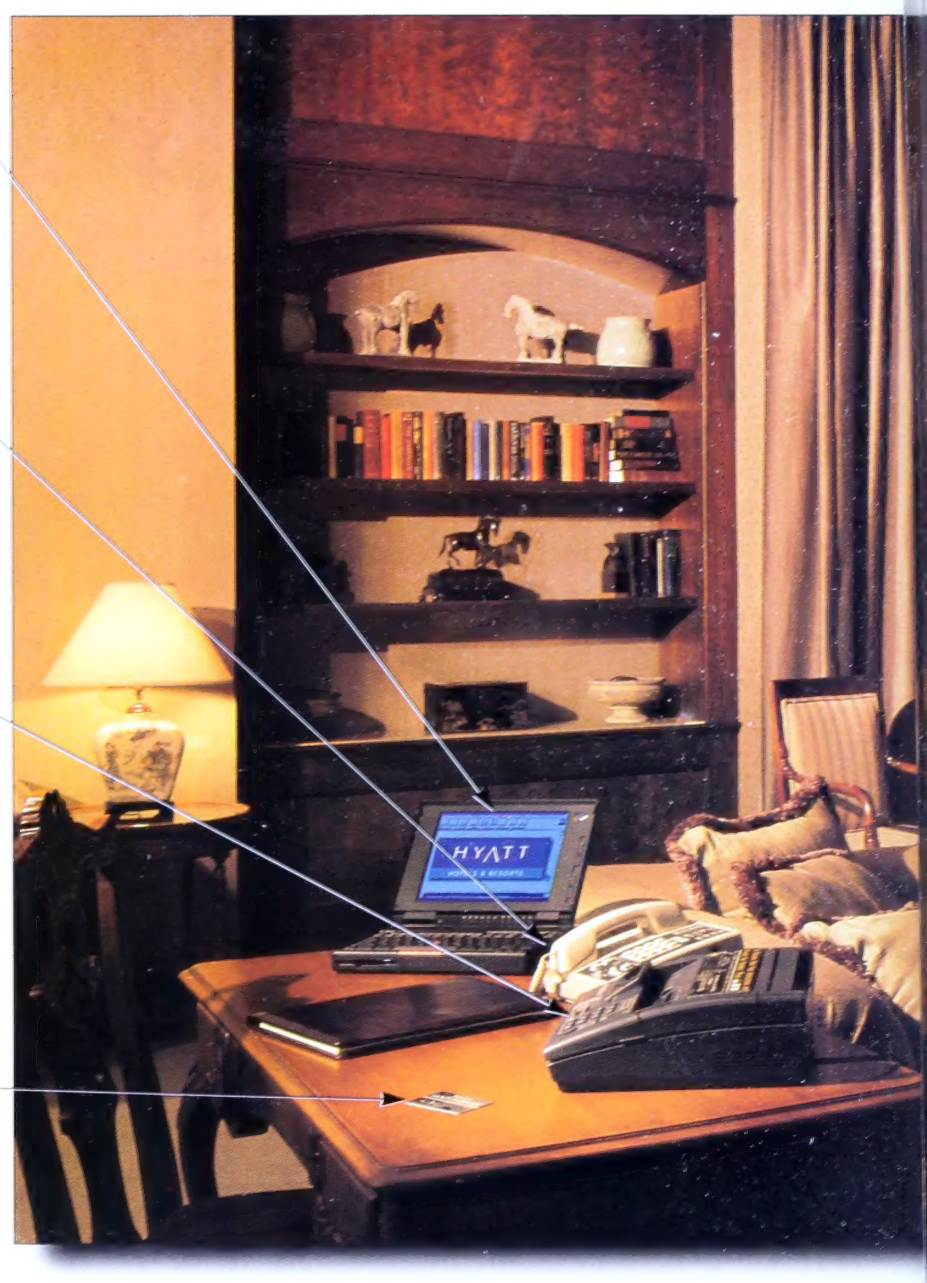

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BusinessWeek
JANUARY 8, 1996

THE BEST

THE 25 TOP MANAGERS

How hot products and smart strategies such as global alliance took this bunch to the top page 50

THE BEST ENTREPRENEURS

In a business climate this nice, with a bit of luck and pluck a business dynamo could become a billionaire twice page 62

THE BEST NEW PRODUCTS

From cycles to kayaks, grea gizmos were mighty grov engines page

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These execs may climb high—or fall hard—in the days to come

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Steve Jobs became a billionaire. Jim Clark did it twice

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From a $105,000, 400-horsepower Porsche to an electric mountain bike

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If you think Washington is paralyzed now, just wait until next year

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1996 INDUSTRY OUTLOOK

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the expansion's sixth year, growth
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m Dewey, meet Peter Drucker

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troit figures to stay on cruise control

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In an otherwise bully year, consumer debt could be a big blot on the ledger

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Low rates mean another super year

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More competition, more consolidation

Up Front

EDITED BY LARRY LIGHT, WITH PAUL ENG

TALK SHOW "The world is full of people whose notion of satisfactory future is, in fact, a return to an idealized past."

— Robertson Davies, the Canadian author of The Cunning Man, *who died at 82 on Dec. 2*

TEA LEAVES, ANYONE?

Once again, Up Front bravely predicts the future. We undertake this foolhardy venture on the basis of what we know about the past. That often can lead one astray, but it's the best we've got.

THE '96 ELECTION. It's Bill Clinton, the Comeback Kid, for four more years. Vilified for much of his first term, he still will outshine his dour GOP challenger, Bob Dole. Right-wing Republicans, uneasy about deal-cutter Dole, will stay home. Ross Perot will mount a third-party foray and skim off more GOP voters. Public dismay over Gingrichian harshness will give the Dems back the House but not the Senate.

STOCK MARKET. Funny thing how the economy and the market usually go up in an election year. Aided by lowering interest rates and ebbing inflation, the Dow should rise moderately, to 5600, by Election Day. Nothing like 1995's performance, however, since that's hard to top.

INTEREST RATES. An eventual federal budget accord—neither party wants to be accused of gridlock—should give the Federal Reserve all the ammo it needs to lower rates some more. Look for the Fed, satisfied that inflation is under control, to reduce the federal-funds rate by a half-point, to 5%, by spring. Then it will lay off, so as not to get tangled up in electoral politics.

MONETARY UNION. The much heralded European Monetary Union will be shelved during a summit this summer. Other than Germany, no European country is close to hitting fiscal targets set up by the Maastricht Treaty for a single currency. These require cutting budget deficits and debt by 1997. As the strikes in France show, the necessary austerity is not popular. Plus, Europe's economies are weakening, which will make achieving the treaty's goals even harder.

FRANCE: *On strike against austerity*

APPLE. Woebegone Apple Computer will sell off chunks of its business, since no buyer wants the whole thing. Look for Oracle's Larry Ellison, Sun Microsystems, or IBM to acquire software. Japan's Canon could be a buyer for the hardware.

SLICE AND DICE: *Apple*

DISNEY. Mickey's run of smash animated films will end with this summer's release of *The Hunchback of Notre Dame*. While not a bust, this flick will do nowhere near the box office of *The Lion King* blockbuster or even the moderate hit *Pocahontas*. In a bid to lure boys and teens, Disney chose Quasimodo's unlovely tale. This downbeat story, though, will turn off traditional Disney fans. Plus, the movie has few of the soaring musical numbers that punctuated earlier efforts.

CHRYSLER. A nasty pro fight erupts as Kirk Kerko an challenges Chrysler. goal is to name his lieuten Jerome York to the boa launch a huge stock buyba and double the dividend. sult: CEO Robert Eaton fe off the billionaire. Eat shunts some of the compan $6.4 billion in spare cash which Kerkorian wanted use for dividends and bu backs—into the more prod tive pursuit of a joint ventu with a foreign auto maker.

THE INTERNET. Net fever v cool off a notch or two. W scads of companies alrea on the Net but profits scar new offerings will tap off. Look for consolidati among the companies prov ing Net services. Most lik winners: America Onli Netscape, Microsoft.

SMARTEST MOVES OF 1995

1. AT&T focused its energies on the booming telecom market by forging plans to spin off its manufacturing arm and its problem-plagued computer unit (the former NCR). The stock has soared since, wiping out all the NCR losses.

2. Early investors in the Netscape public offering profited outrageously. Since going public at 28 last summer, it topped 150 by early December.

NICE HIRE: *A*

3. Colin Powell adroitly managed his public persona with his book tour. By then ruling out a Presidential bid, he avoids the mud of the 1996 primaries. So he's free to be crowned the GOP Vice-Presidential nominee.

4. Kirk Kerkorian advanced his battle to win more influence at Chrysler by hiring its former CFO, Jerome York. York's baleful analyses of the carmaker's finances grabbed investor attention.

5. Caterpillar hung tough and got the United Auto Workers to come back from their 18-month strike, accepting terms they rejected at the outset.

DUMBEST MOVES OF 1995

BAD BOY: *A Calvin ad*

1. Daiwa Bank let a U.S.-based trader run up $1.1 billion in losses. A key regulator at Japan's Ministry of Finance knew about the mess but let it slide.

2. Barings collapsed because it didn't know until too late that Singapore-based trader Nick Leeson ran up $1.4 billion in losses.

3. Newt Gingrich's abrasiveness and vainglory blunted his message. Big example: He said he favored shutting down the government in November partly out of pique that Bill Clinton made him sit in the back of Air Force One.

4. Calvin Klein was forced to withdraw his jeans ads, which used teen models in suggestive poses. Critics accused him of purveying kiddie porn.

5. ABC knuckled under to Philip Morris' $10 billion libel suit over a program about cigarettes' nicotine content that contained one defensible error.

TOUCHY *Newt*

If you're an investor with an appetite for aggressive growth funds, Janus can satisfy your craving.

First, the new news: **Janus Olympus Fund.** Just opened, still small (now's the time for investors who like to get in early). Second, we've reopened Janus Twenty Fund to new investors for the first time in three years. Third and fourth, Janus Mercury Fund and Janus Enterprise Fund: they've both rewarded their investors with impressive returns [see numbers at left].

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	1 Year	Life of Fund
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Janus Mercury Fund	36.08%	28.81%
Janus Twenty Fund	32.66%	15.84%

5 Year 19.54%, 10 Year 16.26%

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Up Front

LET'S PLAY 30 QUESTIONS

Now, let's just see if you've been paying attention. Our pop quiz (no fair peeking at the answers) will reveal the real business-news buffs.

BIG SHOES: *Fuchs*

1. What natural event helped ruin rogue trader Nick Leeson's investing strategy?
2. What is Lou Gerstner's vision for IBM called?
3. What two jobs did Michael Fuchs have at Time Warner?
4. How many parts is ITT splitting into?
5. Name the new CEO of DuPont.
6. Which American company had a major power project canceled by Indian authorities?
7. Who is the recently departed chief of Sony's U. S. arm?
8. What does Steve Forbes want to do to the dollar?
9. Who is the highest-level exec to quit Apple so far?
10. What is former IBMer James Cannavino's new job?
11. Name IPO darling Netscape's chairman.
12. What is the Prowler?
13. Former Simon & Schuster honcho Richard Snyder tried to buy what?
14. What is dethroning Citicorp as the nation's largest bank?
15. Ron Perelman wants to do what with Revlon?

BIG BUST: *Leeson*

16. Which bank has spurned Wells Fargo's buyout overtures?
17. Name Bob Packwood's replacement as Senate Finance Committee chairman.
18. Who wants to sell MGM/UA?
19. Why did CBS's *60 Minutes* yank a segment critical of the tobacco industry?
20. Which newspaper did Times Mirror CEO Mark Willes close?
21. Name Salomon's embattled chief.
22. What is the first U. S. TV series to run on Japanese prime time in eight years?
23. Who is threatening a proxy fight against RJR Nabisco?

TRIVIA QUIZ

24. What company did William Agee last head?
25. Name the theme song for the Windows 95 ad campaign.
26. Who is Michael Eisner's new No. 2 at Disney?
27. Whom did the Grace family oust as CEO of W.R. Grace?
28. Name Leon Hess's chosen successor to head Amerada Hess.
29. Converse bought a sports-apparel maker, then shut it down after 85 days of deteriorating results. Name it.
30. What's the price tag for Bill Gates's new high-tech house on Lake Washington?

BIG IDEA: *Gerstner*

ANSWERS: 1) The Kobe earthquake. 2) Network centric computing. 3) Head of Home Box Office and Warner Music Group. 4) Three. 5) Peter Kroll. 6) Enron. 7) Michael Schulhof. 8) Lock it to gold. 9) CFO Joseph Graziano. 10) President of Perot Systems. 11) Barnes Clark. 12) Chrysler's new hot-rod style car. 13) Western Publishing. 14) Treasurer of Chemical and Chase Manhattan. 15) Take it public. 16) First Interstate. 17) Republican William Roth of Delaware. 18) Owner Credit Lyonnais. 19) Fear of litigation. 20) *New York Newsday*. 21) Deryck Maughan. 22) *The X-Files*. 23) Bennett J. Bigwood and Carl Icahn. 24) Morrison Knudsen. 25) *Start Me Up* by the Rolling Stones. 26) Michael Ovitz. 27) J. P. Bolduc. 28) His son, John. 29) Aptox One. 30) $30 million

YOU MADE THE CALL

THE THIRD ANNUAL UP FRONT Reader Survey is gleaned from 288 responses to our questionnaire, almost half via E-mail. It shows a sober group that's cautiously optimistic and doesn't expect miracles.

READER SURVEY

We asked about job security for the second year in a row. And the answers were pretty close to last year's. In a time of corporate downsizing, the share of those feeling less secure at work rose slightly, from 32% to 36%, while people who are more secure was virtually unchanged. Yet, despite all the gloom and doom we hear about how too few are saving enough for old age, two-thirds project their old-age standard of living to remain as is or get better.

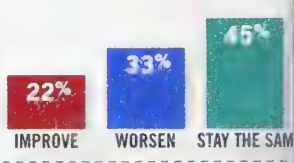
About the stock market, the consensus is for continued good times, with an average prediction of 5754 for the Dow's 1996 high. Most prognostications clustered in the 5251-6000 range. There's no consensus on a favorite stock, though, with name scattered all over. The No. pick is a tie between Microsoft and Intel, with 14 responses each.

On matters not affecting them directly, namely the federal budget readers go for the conventional wisdom. Most name 2002 as the best target date to balance the budget. Newt Gingrich wants to do the deed by then. Now, so does Bill Clinton. There's a tempered optimism on the much ballyhooed Information Highway. While a majority sees the Infobahn as the driving force of tomorrow's economy, skeptics abound: To more than 40% it's just hype.

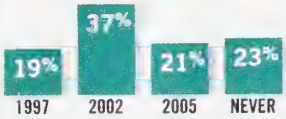
SURF CITY: *So much hype*

● How do you feel about personal job security, compared with your situation last year?

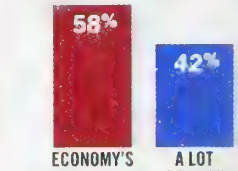
● When you retire, your standard of living will:



● The best target date to balance the federal budget is:



● The Information Superhighway is:



● The high point for the Dow Jones industrial average for 1996 will be:

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Readers Report

HAS CADDY TURNED THE CORNER?

I have received numerous inquiries from your readership concerning "A Caddy that's not for Daddy" (The Corporation, Dec. 18). Despite considerable disclosure of facts and open discussion, your author chose to include her opinions and the clearly biased opinions of our competitors without including any of our perspective.

With regard to our reduction in sales volume: Cadillac's planned and profitable reduction of daily rental fleet sales accounts for much of the reduction in the division's sales from 1989 to 1995. While we chose not to foreshadow our 1995 calendar year forecasts to competitors by providing them for this story, we did provide a yearly accounting of our daily rental fleet reduction statistics (from 32% of total sales in 1991 to 18% in 1994). We expected that disclosure of this plan and accompanying performance would not be omitted from your review of our sales performance.

As for our dealers, you characterized the perception of them as "salesmen in white belts and plaid sport coats" and continued to perpetrate a disservice to our very professional dealer personnel. Our dealers consistently earn high customer-satisfaction scores and were once again rated No. 1 domestic luxury nameplate in a recent J. D. Power & Associates Inc. Sales Satisfaction Survey, second only to Infiniti and ahead of Lexus, Mercedes, Lincoln, BMW, and all other luxury brands.

You also raise questions about our customer demographics. Fundamental changes in our owner demographic profile have resulted from the introduction of the 1992 Seville, Seville Touring Sedan, and Eldorado models. The author accurately quoted the average age of "some model" owners at nearly 70. Specifically, this model is the Fleetwood, which we are eliminating from the model line this year. A fair accounting of our progress would also have noted that the average age of Seville STS owners is 52 years, an average age that has been reduced by six years since the introduction of this model in 1991.

Regarding side air bags, we were disappointed to note that your author chose to omit the rollout of air bags on the 1997 DeVille model, mentioning only the introduction for Catera in mid-1997 and again creating the appearance that Cadillac was behind other luxury manufacturers in the implementation of this technology. The introduction of the side air bags at the beginning of the 1997 model year on the DeVille was made very clear in our interview.

Finally, you refer to us as "an industry joke." In spite of the fact that nine new models have been added to the luxury market from two all-new manufacturers (Lexus and Infiniti) since 1989, Cadillac continues as volume leader in the U.S. luxury market—a title held for the last 46 years. The DeVille remains America's most-purchased luxury sedan—a title held for the past nine years. The Northstar-powered Seville STS is a recognized technology tour de force among automotive critics and enthusiastic owners. The all-new Catera has been reviewed favorably by all of the author's colleagues.

The above-listed facts and many other positive points concerning Cadillac's overall performance were omitted from your story. Our market leadership and product leadership makes preposterous the notion that Cadillac is the brunt of jokes in the industry. To the contrary, our product technology and large loyal owner base are the envy of the industry.

John O. Grettenberger
General Manager
Cadillac Motor Car Div.
Warren, Mich.

Editor's note: Cadillac supplied number on fleet sales only through 19

CORRECTIONS & CLARIFICATIONS

The correct phone number for ordering additional copies of our previous issue, "Where to invest in 1996," is 609 426-5594.

Business Week

A Division of The McGraw-Hill Companies

JANUARY 8, 1996 (ISSN 0007-7135)*** 3457

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d acknowledged that it expected total les to decline by 15% in 1995. Our scription of the negative perception Cadillac dealers focused on younger yers it hopes to attract with the tera and matches the Catera team's n characterization of its consumer search.

Your story on the Catera missed the rk. As I see it, Catera is yet another couraging step as Cadillac transforms elf. Why keep harping on the Cimar-n, unquestionably a Stone Age disas-? Cadillac left the Stone Age long o. Why not mention the Seville Tour- Sedan, Detroit's most exciting world ? What about the national Baldrige ality Award Cadillac received in rec-nition of quality and changes in cul-re? And what about the Northstar stem? You're much too bleak. At 57, I most certainly a Daddy. But Catera t may be the Caddy I've been wait- for—and my boomer son, too.

Dan Panshin
St. Paul, Minn.

Regarding General Motors Corp.'s ns for the new Catera, your article t out a few more mistakes that the dillac Div. has made in past years sides the Cimarron and the Allante. w about the 8-6-4 engines and the ly model Sevilles?

Cadillac had better be satisfied with grandfather image, because any mid--aged luxury-car buff worth his salt uld not even think about a new Cad-c, considering the company's track ord for the past 15 years. Especially th introductory models.

Frank Credendino
Mt. Vernon, N.Y.

ERRORISTS SHOULD NEVER BE NFUSED WITH DISSIDENTS'

I must take exception to your story out Saudi Arabia in your Nov. 27 is-e ("A dangerous spark in the oil lds," International Business). BUSI-SS WEEK played into the hands of rorists by trying to create a link be-een the terrorist car bombing in Ri-dh that claimed the lives of five nericans and the internal situation in r country.

Even though no one knows yet who mmitted this act of murder, your arti- stated that the car bombing "sug-sts once again that internal enemies, t external ones, may now be the ggest threats" to states on the Ara-n Peninsula.

Whether in the U.S., Israel, France, gypt, or Saudi Arabia, people may dis-ree about internal policies. But terror-s should never be confused with dissi-dents. Terrorists kill because they are criminals and murderers. They do not need an "excuse," especially feeble ones such as "belt tightening," as cited in your article.

The "internal situation" that you described did not cause the car bombing any more than the U.S. budget crisis caused the Oklahoma City bombing. Terrorism is a meaningless act. As your story revealed, if you search for "reasons," you will only be led astray.

Bandar bin Sultan bin Abdulaziz
Ambassador
Royal Embassy of Saudi Arabia
Washington

EXPORT DIVERSION, MAYBE. DUMPING, ABSOLUTELY

Regarding "Exports that aren't going anywhere" (Legal Affairs, Dec. 4), I'd feel sorrier for companies whose low-priced exports are being diverted back to the U.S. if they weren't meeting the classic definition of dumping: selling at a lower price in a foreign country than they do domestically.

When a foreign manufacturer sells at a lower cost in the U.S. than it does in its own country, the U.S. Federal Trade Commission is all over them. Are American companies claiming injury when their dumping activities result in the obvious economic consequences? Wait until the other countries' FTC equivalents get through with them.

The reality is that price differentials are extremely difficult to maintain in the global economy. If the law doesn't get you, economics will.

Dick Locke
President
Global Procurement Group
San Francisco

TRAVELERS DOESN'T TRAFFIC IN HARD SELLING

Your recent article on "How Travelers got moving again" (Finance, Dec. 4) stated that CEO Robert I. Lipp "began pushing Travelers homeowners' and auto policies through the PFS network of 100,000 hard-sell part-time agents, who work for commissions far below the typical 15% paid . . ." The article was great, but the connotation that PFS agents employ hard-sell tactics is incorrect. Roughly 80% of the sales force is in fact part-time and does not rely on commissions to make a living. Thus, the basic PFS approach is educational, not confrontational. Part-time PFS agents do not have to make the sale to put food on the table. Hard sell? Nothing could be further from the truth.

David Beemer
Virginia Beach, Va.

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THE STATE OF HUMANITY
Edited by Julian L. Simon
Blackwell • 694pp • $54.95

A PANGLOSS FOR THE MILLENNIUM

No one can accuse Julian L. Simon of thinking small. In his new book, he tackles nothing less than the fate of all mankind. *The State of Humanity*, a massive new volume of essays assembled and edited by Simon, is an attack on the fashionable notion that human progress has stalled. "Just about every important long-run measure of human welfare shows improvement over the decades and centuries, in the United States as well as in the rest of the world," claims Simon in his introductory essay. "There is no persuasive reason to believe that these trends will not continue indefinitely."

This happy assessment is no surprise. In previous books, Simon, an economist at the University of Maryland, has argued the benefits of population growth and immigration, giving him a well-deserved reputation as perhaps the most optimistic economist alive. His argument that humanity is still on an upward trend is backed up by almost 700 pages of hard data and numerous charts and graphs. Simon and his co-authors, including Nobel prize-winning economist Robert W. Fogel, have put together what is probably the single most concentrated mass of upbeat statistics ever assembled, covering virtually every aspect of the human condition, from child mortality to air pollution, from housing and food to natural resources and ozone depletion.

For the most part, the arguments are convincing. We have been warned that the world is about to run out of oil. Not so, Simon points out: Global crude-oil reserves have soared over the pa 15 years, as higher prices have stim lated exploration and new technolo for exploiting existing fields. In 19 the world had about a 30-year supply crude oil at current rates of consum tion. By the early 1990s, though, t world had about 45 years' worth. Not Simon: "Metals, foods, and other natu resources have become more availab rather than more scarce."

The perspective of Simon and his authors is decidedly global. While dev oped economies such as the U.S. ha struggled in recent years, developi countries such as China, Taiwan, a Malaysia have seen explosive incon growth, making this the greatest peri of wealth creation in history. These ec nomic gains have been accompanied other advances, as well. Over the pa 30 years, life expectancy in poor cou tries has soared, from 46 to 63 yea The spread of education in developi countries has been equally spectacul The proportion of children aged 6 to enrolled in school has risen from le than 50% in 1960 to about 70% today

Interestingly, Simon's upbeat vie does not depend on new technology. *T State of Humanity* barely takes noti

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ıeckers feed on parasites in the coats of animals like this impala. They do the impala a service since they rid the animal of irritating parasites.

There are many partnerships in the world of nature that give the impression of being rather unusual at first sight. But at a closer glance, they make a lot of sense, as it becomes quite clear that the partners can benefit each other.

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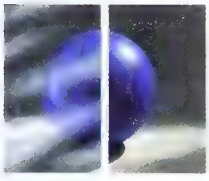

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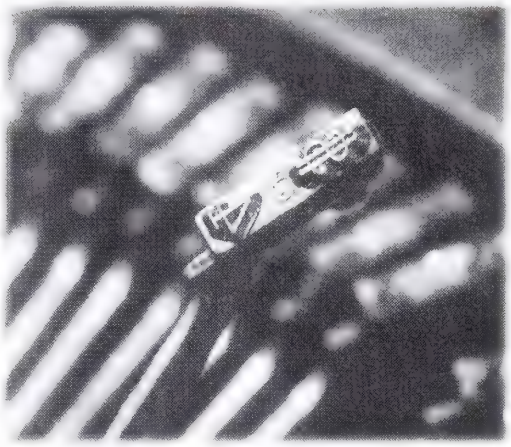

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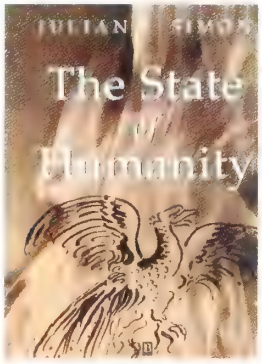
of computers. There is no mention of the Internet, virtual reality, gene splicing, cellular telephones, or any of the other marvels that are supposed to be boosting productivity and improving the modern standard of living.

Instead, Simon bases his forecasts on a simple principle: Assume that long-term trends will continue, in the absence of convincing evidence to the contrary. So if the steady accumulation of knowledge has produced a rising standard of living for the past 200 years, there's no reason to believe that things will suddenly change.

Of course, many would consider Simon's view of the world to be naive. The conventional wisdom is that global overpopulation is inexorably leading to ecological and economic disaster—a modern version of Malthusian misery. "For those who think the future may be a simple extrapolation of the past, there may be some surprises ahead," observes Lester R. Brown, president of Worldwatch Institute, in the forthcoming book *State of the World 1996* (Norton). Brown, as committed a pessimist as Simon is an optimist, argues that the "spiraling human demands for resources are beginning to outgrow the capacity of the earth's natural systems."



Food, especially, will be in short supply, in part because the people of China and other growing nations will demand better diets as they become richer. Notes Brown: "Oil can be replaced with other energy sources, but there is no replacement for food."

The State of Humanity tries to answer each of these negative arguments. Despite the fears, Simon cites statistics from the Environmental Protection Agency to assert that "the air in the U. S. and in other rich countries is irrefutably safer to breathe now than in decades past." Moreover, there is no sign of any widespread food shortages yet. Crop yields have risen as fast as world population. The price of food, like that of other natural resources, is still falling compared with other goods and services.

Simon points out that in every era, there have been doomsayers who see the imminent end of civilization. For example, in the mid-1800s, the British began to worry about running out of coal. Writes Simon: "The great English economist, Stanley Jevons, calculated that a shortage of coal would bring England's industry to a standstill by 1900; he carefully assessed that oil could never make a decisive difference."

Despite the power of its arguments, *The State of Humanity* does have some flaws. The essays are of uneven quality—Simon's own contributions, especially the introduction, are pointed and well-written, but some of the other chapters are confusing and less than helpful. The book also suffers from overkill. One grows weary of being told over and over how everything is getting better all the time.

Moreover, while whining about how the pessimists get more attention than he does, Simon does not acknowledge that scaremongers are often responsible for much of the improvement he cites. The death rate from all accidents, for example, dropped by more than 20% over the past 10 years—thanks in no small part to the consumer-safety advocates Simon professes to deplore. Indeed, it may very well be that alarmism is the only way to stimulate an effective response to large-scale problems, such as global warming and ozone depletion, that require concerted multinational action.

Still, *The State of Humanity* will become essential reading for anyone who wants to put today's policy debates into a larger context. At a time when politicians are locked in a bloody stalemate in Washington and many Americans are disappointed with their lot, it's worth remembering the progress that the human species has already made—and pondering the potential for gains to come.

BY MICHAEL J. MANDEL

Mandel is a BUSINESS WEEK *economics editor.*

BOOK BRIEF

THE DIGITAL ECONOMY
Promise and Peril in the Age of Networked Intelligence
By Don Tapscott
McGraw-Hill • 342pp • $24.95

INTERNET 101 FOR BUSINESS

Surf the Net these days and you soon find, alongside the obscu 'zines and hip cyber hangouts, some the biggest names in business. Koda Aetna, AT&T, Eli Lilly, IBM—each has home page on the World Wide We They and scores of other compani hope online networks can provide direct link to the customer and a who new realm of electronic commerce.

Today, however, most are sputteri along the Information Highway, offeri little more than electronic brochure To get beyond that, argues Don Ta scott in *The Digital Economy*, bus nesses must build fundamentally ne strategies for competing in the ele tronic marketplace. "When informatic becomes digital and networked, wal fall and no business is safe," Tapsco writes. On the other hand, companie that understand the Net will blossom

Tapscott's mission is not to tell exe utives how to craft I-way strategies b to help them grasp the changes the N will bring so they can start plannin This isn't uncharted territory: Tapscot a consultant who has written often c information technology, follows coun less magazine and book writers in pr dicting how the computing, telecommu nications, and media industries wi converge. While he points out the po sibilities, he offers few fresh insight He cites other consultants and quote liberally from business publication Also, many of the companies Tapsco hails as pioneers—Federal Expres Wal-Mart, Levi Strauss—are alread well known for their online strategies

Tapscott does well weaving into on tome the business, social, and educatio al implications of networks. He lays ou privacy and censorship issues, and e plores the Net's potential to change th way people interact with the goverr ment. He also raises important questio about inequality and the need to exten the Net to a broad base of citizens. *Th Digital Economy* doesn't offer solution but it can help executives contemplatin cyberspace to ask the right questions.

BY IRA SAGE

JOHN W. VERITY

T'S FOR YOU ON THE PC

ice calling via the ternet is here and s cheap–but don't ss your phone yet

There's little, it seems, that the Internet doesn't provide: low- electronic publishing, bal E-mail delivery, in- t access to every kind of tal information and ser- . Now, it's promising ee" phone calls be- en any two Net com- ers, more or less, and no more money than usual connection fee. As it turns out, this is ther one of those ernet concepts that n to offer exciting po- ial if not high-quality lts just yet. It's sort ke the idea of finding tever information you d on the Net. Sure, computers are mmed with informa- , but as all Web surf- soon discover, much is trivial.

TING PLACE. Like- e, the Internet can smit speech cheaply, not in a satisfying or y way. Right now, an ernet voice call has little he tone or intimacy of a ular phone call. It's more talking over CB radio. , it costs little to try, and n they work well, Inter- voice calls can be enter- ing and useful. Besides ng money on long-dis- e communications—even oss oceans—Internet ning can enhance comput- games. Eventually, phon- via the Internet may ve as an inexpensive method for training and conference calls.

How to get started? First, you'll need basic Internet knowhow and some patience. For hardware, you'll need a Windows-compatible computer with a 50-megahertz 486 processor, a sound card, a speaker, and a microphone. (Most Internet phone-software packages work only with Microsoft Corp.'s Windows, but there are programs available for Apple Computer Inc.'s Macintoshes and for Unix computers.) A 28.8-kilobits-per-second modem is best, though some packages can work with 14.4-kbs models. Also required is a SLIP/PPP connection to the Internet.

There's already a choice of software. Trial versions are available at no charge directly from the Web sites of several suppliers (table). Even in compressed form, these lengthy programs can take 15 minutes or more to download into your machine. Also, each is programmed to work only for a limited time. VocalTec Inc.'s Internet Phone allows just 60 seconds of calling time, for instance. You're free to take more than one copy—or pay $49.95 for a limitless version. Internet Telephone Co.'s WebPhone program, which was available free prior to Jan. 1, 1996, now costs $49.95.

Each program does essentially the same thing—make your PC's sound card convert the microphone's analog signals into a string of digital packets of data that move separately across the Net like envelopes in a postal system. Depending on the Net's traffic conditions at any given moment, consecutive packets may take different routes through the Net and arrive out of order. At the receiving end, telephony software will try to compensate, but it's often impossible for the program to reconstruct the original signal completely.

None of this software is simple to install or use. There are numerous network and computer parameters to set, and you'll need to plug in specifics about your Internet addressing, for instance. It took me and a friend more than an hour to get VocalTec's package to work. For WebPhone, I sought the supplier's assistance.

TOUGH TALK. Once we had the software installed, we found out just how different from conventional telephone calling Internet phone setups are. The sound is choppy, syllables drop out of words, and it can take several seconds for voices to traverse the Net. Each party must take turns speaking—and they must be using the same brand of software. You must either arrange a time to converse or scan your supplier's online directory to find others around the world who are online and looking for conversation. Directories often list people's preferred topics of conversation, which range from the personal to lofty technical matters.

Which software to choose? As the first to market, VocalTec's package has become the most popular. Internet Telephone's WebPhone looks the best—like a futuristic telephone with lots of point-and-click buttons. Quarterdeck Corp. plans to enhance its WebTalk with a variety of multimedia tools to help people collaborate over the Internet. You can keep up with the technology's rapid evolution by seeing what enthusiasts post to the independently run Voice on the Net E-mail list: Send the message, "subscribe von-digest," to majordomo@pulver.com.

For now, Internet telephony reminds me of the dancing elephant in a circus: One is more impressed that it can dance at all than with the dance itself. But at this stage, teaching the Internet new dances is really what it's all about.

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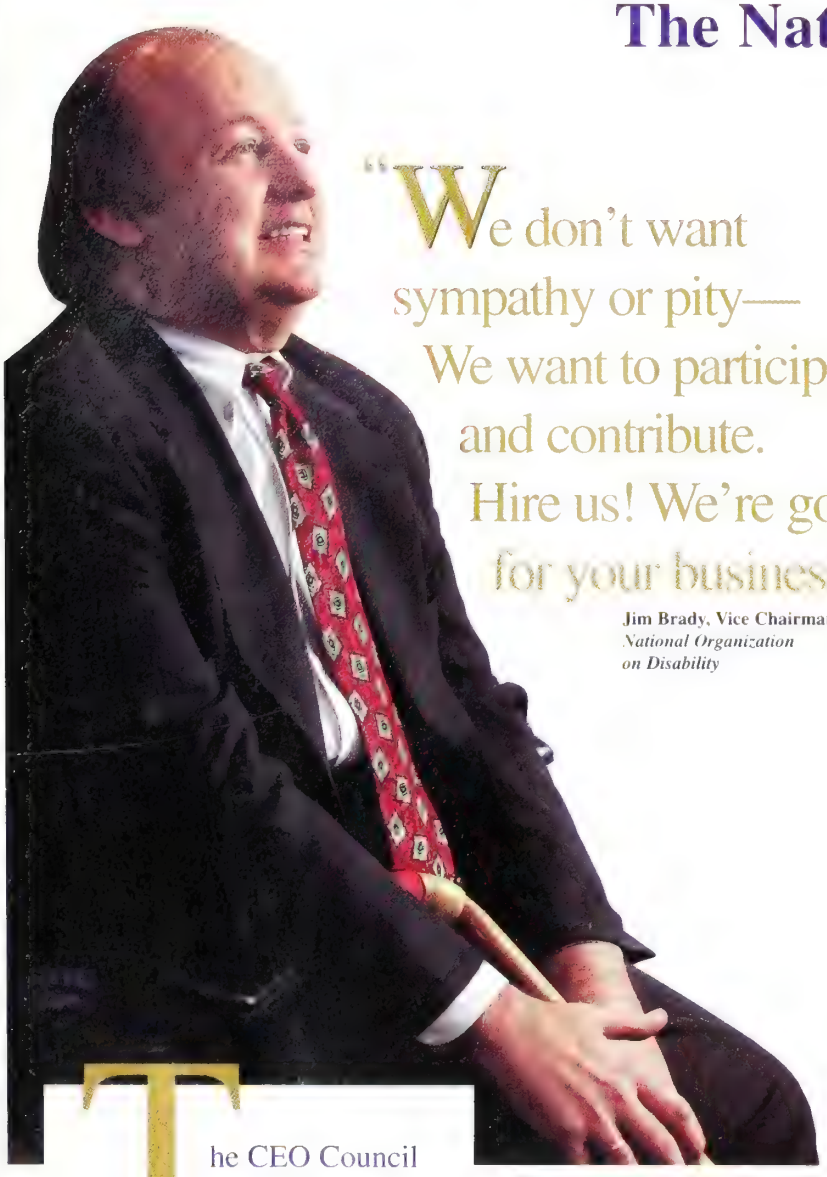

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BY PAUL CRAIG ROBERTS

WHY IS THE U.S. SETTLING FOR STUNTED GROWTH?

ANATHEMA: Liberals would rather put the brakes on growth than have a fast expansion based on supply-side principles

Economic growth has fallen on hard times. The budget struggle between Congress and the Clinton Administration has been partly over whether the economy will grow 2.3% annually or 2.5%. Federal Reserve Board Chairman Alan Greenspan has hinted that even this slow growth might not be possible without a balanced budget.

It was not always so. In the postwar era, growth was a liberal mantra. Not even inflation-shy Republican Administrations could withstand its imperative. The Ford Administration, for example, forecast a growth rate of 5.98% in average annual real gross national product for the 1976-80 period. The Carter Administration brought us into the 1980s with a 4.7% average annual real GNP growth projection for 1979-83.

The attitude toward growth changed remarkably in 1981, when the Reagan Administration forecast a 3.8% annual rate of real GNP growth from 1981 to 1985. The forecast was paltry compared with those for earlier periods and was no higher than what the economy achieved from 1976 to 1980. But the hyperbole flew fast. Reagan's forecast was denounced as a "rosy scenario" that "lies far beyond the limits of any past experience in this country or any other industrial democracy" (*The Washington Post*, Mar. 9, 1981).

COOLED PASSION. What happened in such a short time span to make modest economic-growth projections unwelcome? Environmental hysteria connecting growth with pollution took a toll, as did the rising inflation that had accompanied growth in the 1970s. But among macroeconomists themselves, the cooled passion for growth may have reflected the change in the way it was being pursued.

In the postwar era, prosperity-peddling Keynesians connected economic growth with the growth of government. True, in the Keynesian model, a tax cut that increased the deficit would raise aggregate demand and economic growth, but the tax cut multiplier was less than the government-spending multiplier. That is, if economic growth was the goal, more government spending was the efficient way to achieve it. Keynesian economics was a political success because it merged economic growth with liberal compassion and the propensity of politicians to build spending constituencies. Moreover, the Keynesian model relied on a proactive government to manage aggregate demand and produce full e ployment. Policymakers found this to be more gratifying approach than laissez-faire

Reagan's growth program was unpopu with macroeconomists because it was r premised on the growth of government. I deed, Reagan wanted to curtail the growth government, while increasing economic centives to individuals. This cut to the en tional core, and liberals who couldn't g enough "Keynesian" growth were horrifi at the prospect of "supply-side" growth.

For many, supply-side economics has even worse strike against it. It maintai that fiscal policy works not by increasing a gregate demand, but by raising aftertax r wards for work and investment. Supply-si economics not only tolerates market-bas income differences—it also links tax poli with productivity growth and shows the hi cost of using taxes to level incomes.

Liberal economists have responded not l resurrecting Keynesian demand manag ment—an impossible task—but by deemph sizing growth. One way of doing this is to a gue that regardless of policy, the econon cannot grow any faster than its long-ter average of 2.5% annually. Liberals then na rowly limit economics to "fairness" issue For example, Paul R. Krugman, an econ mist at Stanford University, says that with long-term growth potential of 2.5%, it is poi less to increase incentives when the only e fect is more economic inequality.

A downsizing of growth ambitions requir harsher cutbacks in welfare and entitlemen in order to contain the deficit or balance t budget. It also means that policymakers ca not rely on income growth to compensate f the slower growth in government prograr or on job growth to absorb the inflow of leg and illegal immigrants. The social and politic implications of slow growth may well pro more unpalatable than "greed."

From 1982 to 1989, the U.S. econom grew at an average annual rate of 3.7%. Tl new "2.5% inevitable growth school" ma argue either that these seven years of abov inevitable growth occurred at the expense future growth or compensated for belov inevitable growth in the past. But the fa remains that people experienced 3.7%, n the long-run average. The electorate liked i and the Washington policymakers who toc it away are history.

Paul Craig Roberts is John M. Olin Fellow of the Institute for Political Economy and Distinguished Fellow of the Cato Institute in Washington, D.C.

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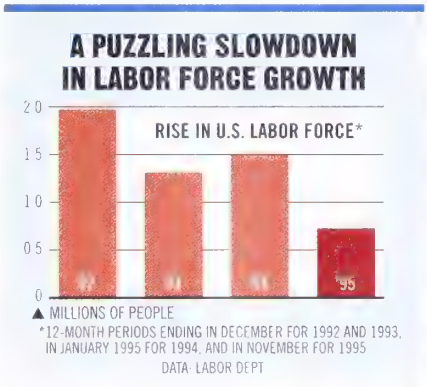
BY GENE KORETZ

FED FEAR OF THE JOBLESS RATE

It may be a faulty inflation signal

Though they welcome the Federal Reserve's latest cut in short-term interest rates, economists Mickey D. Levy of NationsBanc Capital Markets Inc. and Joseph Carson of Dean Witter Reynolds Inc. both believe that Fed policy remains far too restrictive in the face of growing economic weakness. As they see it, the largest roadblock to a substantial easing of monetary policy may well be the Fed's unjustified concern regarding the low unemployment rate.

Fed officials, says Levy, tend to believe in a so-called natural rate of unemployment—that is, a rate at which labor markets are so tight that further declines would spark rising inflation.



Though estimates of that rate have varied from 4% in the 1960s to 6.5% in the 1970s, the current level is presumed to be just below 6%—placing November's 5.6% jobless rate in the danger zone.

Levy argues, however, that productivity progress by U.S. business combined with the Fed's enhanced inflation-fighting credibility have effectively lowered the natural rate of unemployment well below the 5.5%-to-6% range. By reaping productivity gains from restructuring and more flexible use of labor (including contingent workers), as well as from increased investment in technology, says Levy, business has improved its resiliency in labor markets and boosted its leverage in wage bargaining.

Meanwhile, growing job insecurity has made employees more docile. And the Fed's tough anti-inflation stance has curbed employers' ability to pay for wage hikes by raising prices. All of which, says Levy, suggests that today's 5.6% jobless rate is far from a danger signal of impending inflation.

For his part, Carson notes that the meager 607,000 rise in employment over the past 12 months (as measured by the Labor Dept.'s survey of households) was matched by unusually sluggish labor force growth of just 724,000 people. This is only half of the 1.1% growth in the labor force in 1994 (chart), which was right in line with Labor Dept. projections.

Carson attributes this sharp drop in labor force growth to declines in labor force participation by 20-to-24-year-old and 55-to-64-year-old males. He speculates that poor job prospects in 1995 inspired more young workers to stay in school, while continued downsizing eroded the ranks of older workers. In any case, he says, "the thing to remember is that the unemployment rate would be a half a percentage point higher if the labor force had expanded at its trend rate."

Either Levy's or Carson's analysis may explain why inflation has stayed so low with 5.6% unemployment. If, as seems likely, they are both right, the Fed has more than ample room to ease aggressively in the months ahead.

WHAT'S STALLING MONETARY UNION

Europe's economies are out of sync

At first blush, the wave of European interest-rate cuts touched off by the Bundesbank's latest move would seem to suggest that economic convergence is growing. Christopher Widness of Chemical Securities Inc. points out, however, that despite the synchronous rate cuts, the differences between inflation rates (and interest rates) have actually widened. A year ago, for example, French inflation was nearly a percentage point lower than German inflation. Today it is higher. And the gaps between German inflation and inflation in Spain and Italy have grown (chart).

The irony, says Widness, is that in many countries, such as Italy and Spain, fiscal restraint could boost inflation as sales tax hikes feed into the price indexes and inspire wage pressures. And that spells increased political strains that could short-circuit progress toward economic convergence and monetary union.

A MILESTONE FOR BLACK FAMILIES

Fewer out-of-wedlock births

As reported by *The Numbers News* newsletter, black families in America have made significant progress in at least one key area in recent years: Birthrates among unmarried black women—including teenagers—declined in 1993 for the fourth year in a row. The birthrate fell from 90.7 per 1,000 unmarried black women age 15 to 44 in 1989 to 84.0 in 1993. By contrast, the birthrate among unmarried white women, though far below that of blacks, continues to rise sharply—from 30.2 in 1989 to 35.9 in 1993.

WHEN LAWYERS ARE LOOKERS

Attractiveness boosts earnings

Other things being equal, better-looking lawyers make more money than their unattractive colleagues. That's the implication of a new study that looks at how law school graduates of the 1970s fared in labor markets in subsequent years. In the study, economists Jeff E. Biddle of Michigan State University and Daniel S. Hamermesh of the University of Texas developed attractiveness rankings based on class photos of students of a top law school and then used survey data to gauge their career progress five and 15 years after graduation.

The results indicated that attractive male attorneys (there were few women in the group studied) made more money than plain or homely attorneys after five years of practice, and the gap widened over time. Further, more of the attractive group tended to become litigators, a specialty where good looks are a likely asset, and to work in the higher-paying private sector, where client relationships have a larger effect on earnings.

Interestingly enough, the researchers found little payoff to attractiveness among law school graduates of the 1980s. And while good looks boosted the chances of males grads of both the 1970s and 1980s being offered a law firm partnership after only five years of practice, they actually lowered the chances of early partnership for young female lawyers.

BY JAMES C. COOPER & KATHLEEN MADIGAN

FROM CHRISTMAS BLAHS TO NEW YEAR'S EASE

U.S. ECONOMY While Congress and the White House play their politi- games over the budget, they seem oblivious to the ngers of testing the patience of the financial markets. th so much anticipation for deficit reduction already ced into the markets, Wall Street had better get ne good news from Washington fast, or another 102- int tumble in stock prices and a sharp sell-off in nds like those of Dec. 18 could be in the making.

For now, at least, the markets have taken solace m elsewhere in Washington: the Federal Reserve. e Fed's Dec. 19 quarter-point cut in short-term inter- rates has soothed the markets' edginess, not so ch because of that one snip but because it now ks as though more policy easing is on the way.

The strongest hint of that is the reason given by the Fed for its latest cut. Chairman Alan Greenspan cited not a soft economy but inflation that was "somewhat more favorable than anticipated." More important, he noted "an associated moderation in inflation expectations." The two-point drop during the past year in long-term bond yields, ich incorporate anticipated inflation, bears that out. f such expectations are indeed down, the Fed cannot tify holding its overnight federal funds rate nearly ee full points above the rate of inflation, in light of historical average of only about 1¾%. What Green- n is saying is this: Against a more sanguine attitude ard future inflation, real short-term rates are simply high.

Moreover, these expectations of lower inflation are fleeting. They are set to stay down amid continued dest economic growth, an eventual budget deal, a onger dollar, and a new order of technology-driven npetitiveness in Corporate America.

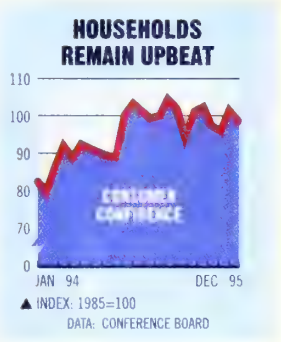
E IMPACT of these structural forces is clear in the vember consumer price index, which was flat for first time since the end of the last recession in rch, 1991. The core index, which excludes the vola- energy and food sectors, rose a scant 0.1%.

Through November, annual CPI inflation was run- g at 2.6%, the same as in 1994, and it seems likely have ended 1995 very near that pace. Back in July, Fed's own forecast projected that inflation for the year would be much higher, between 3.1% and 3.4%.

Even service inflation, widely anticipated to be the first area to register a speedup, has remained modest, at about 3.4% for most of the year. Meanwhile, goods inflation, at 1.5% in November, is hardly on the radar (chart). However, that low rate is the result of deep discounting by many retailers, which threatens their profits—and for some, their very existence.

Retailers' dreary little Christmas provides additional support for a winter rate cut. Despite the expected last-minute surge, stores still reported pretty dismal sales in December. Rampant price promotions to lure shoppers subtracted from dollar revenues. The early winter weather in some parts of the nation only added to the problem. The *Johnson Redbook Report* said December sales at department and discount stores through Dec. 23 were 2.4% below November sales.

Lifeless sales mean that yearend profits will be a disaster for many retailers, and the consolidation process already wracking the industry will accelerate. More chains, especially regional discounters and apparel stores, are likely to seek bankruptcy protection.



The resulting liquidations could well lead to further downward pressure on goods prices. If so, an actual decline in the monthly CPI in any of the coming months cannot be ruled out.

This lack of price pressure should bolster the strong low-inflation sentiment in the bond market. And given the Fed's statement on inflationary expectations, low long-term rates will give the central bank even more room for another rate cut.

DO THE RETAIL WOES mean that the economy is tanking? Not necessarily. Much of the profits decline stemmed from price cutting, so sales on an inflation-adjusted basis should look somewhat better. Also, consumer confidence, while down slightly in December, remains at the level it has held for most of 1995 (chart).

Moreover, according to one top Fed official, the central bank is aware that the reports from individual retailers do not match the data used to calculate the Commerce Dept.'s retail sales figures. And those retail numbers do not include service purchases, which have remained healthy in recent months.

But while consumer buying is not as dramatically

weak as the dour reports from retailers would suggest, demand will still be no better than modest. One reason is that in early 1996 consumers will have to contend with their holiday credit-card bills.

THE RESULT WILL BE continued pressure on industrial output and employment, as businesses adjust their inventories to more desirable levels. That scenario should translate into unexciting economic growth in the new year—another reason the Fed will have room to ease policy further.

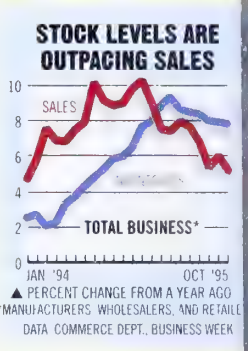
In October, inventories held by manufacturers, wholesalers, and retailers rose 0.6%, but sales tumbled 0.4%. During the past year, the annual growth rates of both inventories and sales have been slowing, but the pace of sales has slowed faster (chart).

That disparity is the chief reason for the continued sluggishness in the industrial sector. Industrial production in November rose a tepid 0.2%, following a decline in October. Output for the fourth quarter is on track to rise even more slowly than the lackluster 3.2% annual rate posted in the third quarter.

The international economic climate is also conducive to rate cutting. Even before the Fed's Dec. 19 move, the British Treasury and the German Bundesbank had trimmed rates in the face of slower economic growth. And following the Fed, the Bank of Canada eased monetary policy as well.

Other European central banks followed the Germ lead, as growth throughout Europe appears to be slo ing, leading most private forecasters to cut their proje tions for 1996 European growth. Almost all industri ized nations reported weak holiday sales.

Consequently, the dollar should be able to maintain its recent trend of appreciation against the German mark and the Japanese yen, even in the face of further rate reductions by the Fed. The greenback will get some added support when a budget deal rolls in from Washington—whenever that may take place.



That delay, however, will not hamstring monetary policy. In the recently r leased minutes of the Fed's Nov. 15 meeting, the centr bankers agreed that the Fed "could not freeze its po icy options while it awaited the outcome of a pr longed federal budget debate."

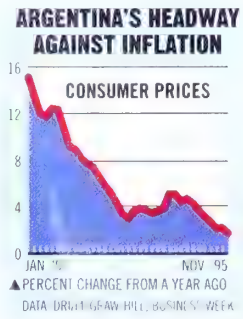
Now that Shutdown II has stretched to recor length, the Fed's refusal to be tied to the politic wrangling means that economic and inflationary for es will set the course of monetary policy in ear 1996. And right now, those forces point to furthe easing ahead.

ARGENTINA

A HARD-WON VICTORY IN A SOFT ECONOMY

After a dismal 1995, Argentina is poised for an expansionary 1996. And that growth will pave the way for fiscal improvement and a stable currency.

The latest sign that Argentina is coming out of recession came from the Latin America Research Fund. The private agency reported that demand for industrial goods rose again in November. Purchases have been increasing since hitting a three-year low in August, with capital goods leading the gain. In addition, in its semiannual survey the government said that the unemployment rate slipped to 16.4% in October, from a record high of 18.4% in May. However, only part of the drop is the result of job growth of 40,000 new slots. The rest came from workers dropping out of the labor force.



Argentina's economy likely fell by 2.5% in 1995, but the government is forecasting growth of 5% in 1996. Private economists expect a more realistic 3% advance this year. Economic growth should be fueled by lower interest rates, a stronger peso—thanks to its link to the rising U.S. dollar and low inflation—and inflows of foreign funds. Already, prospects of better corporate profits have lifted the stock market in recent weeks.

Economic growth will keep the markets rising. And it will help the government balance the budget in 1996, after Argentina's $2.4 billion deficit in 1995. To raise revenues, Congress hiked the cigarette tax by 7% on Dec. 21.

Argentina's slump was the result of an austerity program to fight hyperinflation—a battle that has succeeded so far. Consumer prices were up 1.7% from a year ago in November (chart). Inflation is on track to rise between 1.5% and 1.7% for 1995, the lowest rate on record. In 1989, Argentine inflation ran at a stunning 5,000%.

The International Monetary Fund has blessed Argentina's economic and fiscal progress, saying it would lend Argentina $380 million this year. That influx of funds—along with private money attracted by the rising stock market—is added insurance that Argentina's economy will grow in 1996.

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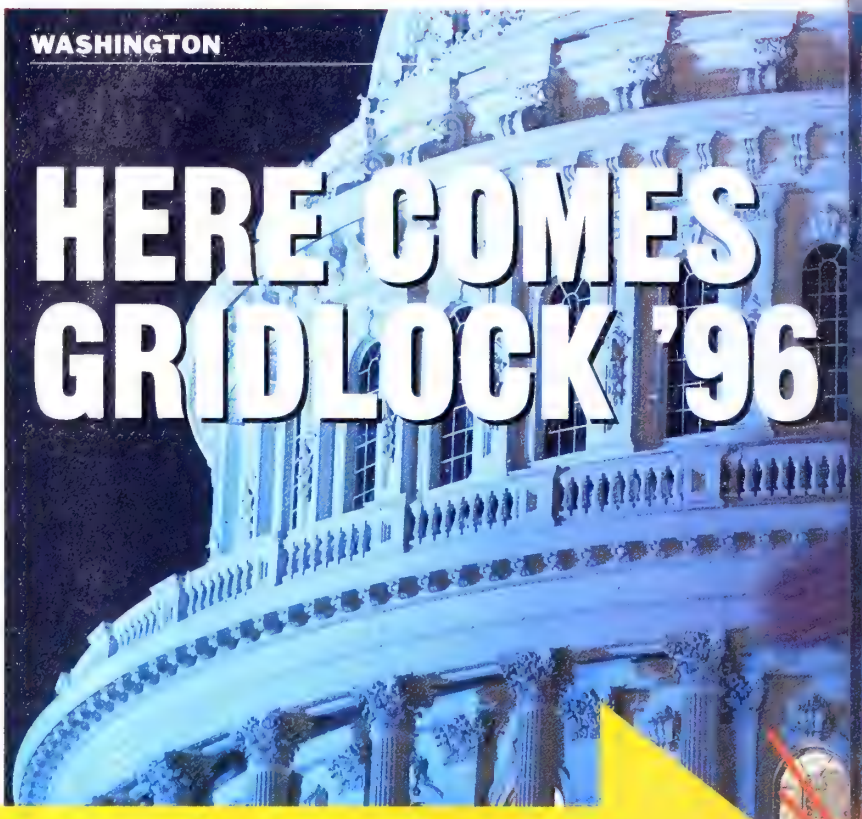
WASHINGTON

HERE COMES GRIDLOCK '96

Dug-in liberals and GOP zealots spell election-year paralysis



If you liked the partisan battles of '95, you'll love what's in store for '96

TAX REFORM

Expect early skirmishing over GOP plans to overhaul taxes. Republicans will push competing plans for a flatter income tax. The Democrats want reform that retains progressive tax rates and closes corporate loopholes.

REG-SLASHING

Republicans will renew calls for legislation that gives companies relief from lawsuits and environmental mandates. The Democrats, allied with Republican moderates, will again attack reform proposals as extreme.

Citing irreconcilable differences with his Republican foes, President Clinton vetoes appropriations bill after appropriations bill, leaving large chunks of the government to run on fumes. A bitter budget impasse shutters the federal bureaucracy for the longest stretch in history, forcing the Treasury to resort to creative accounting to fund essential arms of government. Voters increasingly dismiss the capital caterwauling as the latest example of Washington's childishness. Actually, there's another way to describe the capital's escalating political brawl: dress rehearsal.

As the 1995 legislative season draws to a rancorous close with the fate of a budget-balancing accord, welfare reform, and other key legislation unresolved, the tone is being set for next year's policy struggles. In the best of times, an election-year Congress can be expected to elevate political theatrics over substance. But the ideological differences between dug-in Democratic liberals, GOP hardliners, and a President obsessed by reelection will ensure that next year's Congress—and any chance business had for advancing the solid legislative gains of '95—will be stymied by paralyzing political gamesmanship.

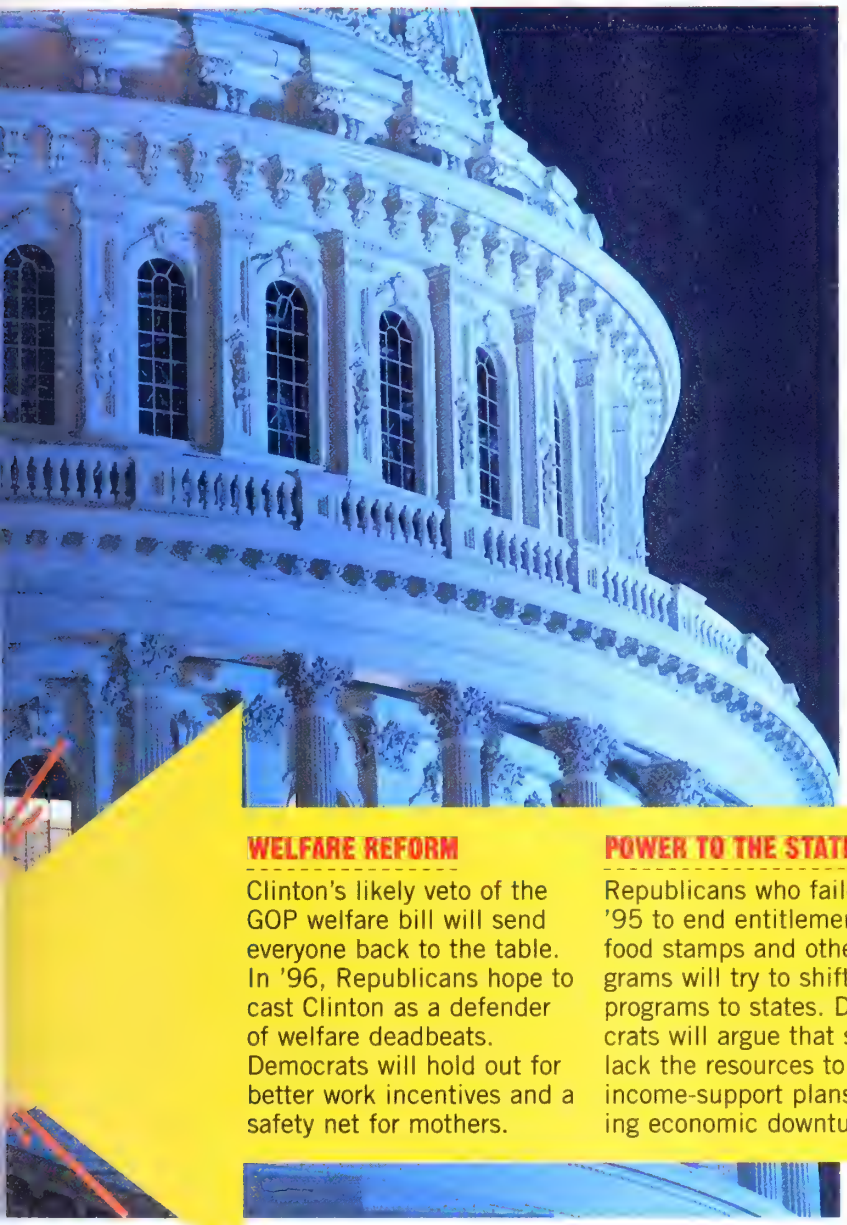
Even as GOP and Administration budget negotiators warily convened for a round of post-Christmas talks, the realization was growing that after months of Republican dominance, Washington has once again become Gridlock City. "We're ready to kill each other already," laments a Democratic leadership aide. "It can't get any worse—can it?"

Actually, it can, and it will. Bolstered by his success at using the Medicare debate to paint Republicans as extremists, President Clinton plans to continue his political jiu-jitsu in 1996. The new target: a GOP flat-tax proposal that the Administration will cast as a boondoggle for wealthy investors. Says a Clinton adviser: "Medicare was just a dress rehearsal for what Republicans are in for when Democrats start in on the 'tax giveaway for the rich.'"

HANGING TOUGH. If Clinton is spoiling for another fight along class lines, he's sure to find one with a combative group of Hill conservatives who are not letting House Speaker Newt Gingrich's plunging popularity cool their fervor. The freshmen have hardened GOP resistance to a budget-balancing accord and promise to make more trouble next year by redoubling attacks on the welfare state.

The hang-tough tactics "haven't been marching orders from Newt Gingrich," says rookie Representative Steve Largent (R-Okla.). "We came in here with our name on the dotted line." Another freshman Representative Zach Wamp (R-Tenn.): "We've been called radical and extreme, but I think we're right out of the heart of America." Still, business leaders worry that the freshmen's all-or-nothing approach is overly antagonistic. "The war is worth fighting," says Amway President Dick DeVos. "But it shouldn't be done stupidly."

To appreciate just how complicated 1996's legislative equation will be, take a short stroll across the Capitol from



WELFARE REFORM

Clinton's likely veto of the GOP welfare bill will send everyone back to the table. In '96, Republicans hope to cast Clinton as a defender of welfare deadbeats. Democrats will hold out for better work incentives and a safety net for mothers.

POWER TO THE STATES

Republicans who failed in '95 to end entitlements for food stamps and other programs will try to shift the programs to states. Democrats will argue that states lack the resources to fund income-support plans during economic downturns.

THE RIGHT'S AGENDA

Under heavy pressure from conservative freshmen, House Speaker Newt Gingrich will allow votes on new abortion restrictions and a repeal of the assault-weapons ban. Democrats will try to thwart both measures.

the foxholes of
House GOP guer-
ıs to the placid quarters of Senate
ority Leader Bob Dole. The Repub-
n front-runner will pursue his own
nda—and none of it includes riling
ential voters, Gingrich-style. Dole
ıs a light Senate schedule for the
t three months of '96, which will
e him lots of time to wrap up the
ination. Concedes one senior House
fer: "All we're going to get done
ınd here is the minimum must-pass
nda."

Even a minimal Hill agenda could fall
im to gridlock. Aside from monitor-
preliminary hearings on radical sim-
cation of the tax code, business is
nest on winning regulatory relief
n nuisance lawsuits, environmental mandates, and overeager regulators who don't weigh the potential economic impact of new rules. The outlook for sweeping change is even gloomier. For starters, Dems will continue to score political points by portraying GOP reformers as too cozy with polluters and overly beholden to corporate benefactors. And House and Senate Republican moderates will continue to line up with Dems against GOP radicals. The bottom line for business: little progress in '96.

On another front of interest to business lobbyists—political reform—bipartisan attempts to limit the role of organized giving in political campaigns seem likely to be thwarted by the leaders of both parties. Newly triumphant Republican leaders are shaking the corporate money tree hard and don't want to give up their advantage. Democrats, meanwhile, remain hooked on reforms that include taxpayer subsidies vehemently opposed by Republicans. The prospect: Look for superficial reforms, at best, and torrents of pious rhetoric.

DEEP BELIEFS. GOP plans to dismantle New Deal social programs by returning responsibility to the states will face tough sledding, too. Already, GOP moderates have quashed reformers' efforts to turn food stamps and the school lunch program into state-run block grants. And Clinton's attack on GOP schemes to shift Medicaid to state capitals is just a preview of a '96 Democratic assault that charges Republicans aim to shred the social safety net. The outlook: Although Clinton may yet cut a deal on a proposal to end the federal guarantee of open-ended welfare benefits, other GOP "devolution" initiatives will languish.

At bottom, deeply held partisan beliefs frame this running debate about the role of government. But the tactics of the combatants are disturbing the American electorate. In December, the Harris Poll's annual "alienation index" hit a 30-year high. And an Associated Press poll released on Dec. 26 found that 29% of those surveyed said neither political party addresses their top concerns. That's why the return of Washington gridlock will spur demands for new political options—whether it's Ross Perot's infant Reform Party or another movement.

"People are concerned by all the posturing and shifting of blame," says New Hampshire pollster Richard Bennett. "All politicians are going to pay the price." Perhaps. But until a resurgent Bill Clinton, unrepentant Gingrichites, and comeback-minded Democratic liberals pause to assess the long-term costs of their scorched-earth tactics, don't look for any break from gridlock politics. All sides are having too much fun gumming up the gears of the American political machinery to stop now.

By Richard S. Dunham, with Lee Walczak, in Washington

TELECOMMUNICATIONS

TELECOM: WHAT HAPPENS WHEN THE WALLS FALL

Once reform passes, a frenzy of pair-ups is sure to follow

They might as well be ringing a starting bell on the Capitol steps. Washington's long revamp of telecommunications law is just about finished. The message most telecom companies hear ringing loud and clear: Let the deals begin.

On Dec. 20, House and Senate conferees finally hammered out a compromise that would allow Baby Bells, cable-TV operators, and long-distance companies to invade one another's turf. It would also permit companies to own more radio and TV stations than is now permitted. Thorny details, such as how much to relax curbs on foreign ownership of U.S. companies, remain to be determined. But says Representative Rick Boucher (D-Va.): "All the core issues have been settled. This will be landmark legislation."

SEIDENBERG AND SMITH: *A long-distance joint venture?*

Once the bill is passed, probably by early 1996, a swarm of mergers, alliances, and joint ventures seems inevitable. That's because most of the rigid regulatory barriers between segments of the industry will be gone. Now, says Robert Barada, chief strategist for San Francisco-based Baby Bell Pacific Telesis Group: "Technology and customer demand are going to break down the walls."

"LOOKING." Which companies are likely to pair up? Bell Atlantic Corp. and Nynex Corp. may be among the first, either through a complete merger or—more probable—a joint venture on long-distance service. Bell Atlantic CEO Raymond W. Smith and Nynex chief Ivan Seidenberg already have joint ventures going to provide cellular phone service and, with PacTel, develop programming for cable TV. Indeed, a Bell Atlantic spokesman calls a long-distance joint venture with Nynex "a real option." Adds Nynex Telecom Group President Richard A. Jalkut: "We are looking at all possible combinations."

Teaming up to challenge AT&T, MCI Communications, and Sprint in the long-distance market would make good business sense for the two Northeast Baby Bells. The Bell Atlantic and Nynex regions account for $20.5 billion of the nation's annual $73 billion long-distance bill (charts). A merger would give the two Bells the marketing and technical firepower needed to compete for customers. Just pooling their ad budgets—Bell Atlantic alone spends about $105 million yearly on all advertising—would challenge the $1 billion the Big Three long-distance carriers spend promoting their phone services.

Who's next? Analysts expect each Baby Bell to eventually link up with at least one other. Among the predicted pairings: Pactel and U S West, San Antonio-based SBC Communications a BellSouth, and, perhaps, Chicago-bas Ameritech with Bell Atlantic and N ex. GTE Corp., with phone lines sc tered around the country, is expected find allies, too. Among other thin partnerships would help the Bells bet tap international markets. Team-ups Southern Baby Bells, for instance, co move into Latin America, while We ern outfits could target t Pacific Rim.

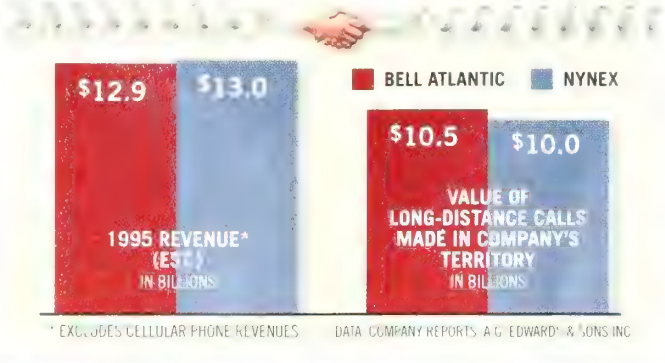
CULTURE CLASH. Long-d tance providers, too, shou find dealmaking irresistib Pacts with the Baby Be would eliminate the need duplicate local networks wh providing potent marketi partners. Analysts say M Communications Corp. is natural ally for a Bell Atla tic-Nynex team, for instan But long-distance carriers looking further afield as w Since late 1994, Sprint Co and cable operators Tele-Co munications, Cox Cable, a Comcast have been explori ways to leverage phone a cable-TV operations into advanced co munications systems. One caveat: A c ple of years ago, Bell Atlantic sought merge with TCI in a failed deal that c firmed Smith's empire-building aspi tions. That failure showed how tou it can be to join the go-go cable wo with the more conservative Bells.

Another caveat: Analysts figure AT will probably avoid cutting deals w Baby Bells because it won't want to accused of recreating Ma Bell. It m team up instead with, say, Time Warr Inc.—already a rumored negotiati partner—to use cable lines for lo phone service. That would dramatica blur the old lines between segments the telecom industry—and set the sta for even more radical change. The de to come will be "complex, multifacet multidimensional things," sa Tony Ferrugia, a telecom an lyst at A.G. Edwards & So Inc. in St. Louis.

In the end, the rewir telecom biz probably will clude far fewer players w will deliver better service a offer bold innovations. Ma B won't exactly be coming ba together after 12 years, b some of her offspring almo certainly will.

By Joseph Weber in Phi delphia, with John Carey Washington

TWO PHONE GIANTS' LONG REACH



PPLE: ANOTHER BOUT F BAD TIDINGS

rofit pressure may bring layoffs and suitors

Spindler seems willing to sacrifice margins for market share. But can Apple afford it?

Mike Spindler just can't get a break. Instead of celebrating the blowout sales he expected this Christmas arter, Apple Computer Inc.'s CEO is acing for a very rough ride. In mid-cember, the company warned of a pos-le loss during the period, and analysts r the worst—layoffs, projects killed, ybe more losses. Some even say Apple l have little choice but to sell off parts, ot all, of the business. And there are ain rumors that Spindler's job is in pardy. Says Robertson, Stephens & . analyst John T. Rossi, who doesn't esee profits again until next fall: "Ap-is in a tougher spot than it's been in a long time."

The reason? Banking on a strong sea-n, Apple pumped up production by ut 30%. To move its many Macintosh dels, the company slashed prices. Si-ltaneously, it faced a shortage of prof-le high-end models. To make matters rse, Apple was slammed by a vicious ce war in Japan. The net result: On c. 15, Apple announced that its unit es and revenue for the Christmas arter were running above last year's el but below internal forecasts. Dean tter Reynolds Inc. analyst Eugene G. zer now expects Apple to report a million loss for the quarter, down from 178 million profit on sales of $2.8 bil-n for the same quarter a year ago. zer figures Apple's gross margins for period slipped to a tiny 18.2%.

EDIT WATCH. Apple has gained market re worldwide, hitting 9.3% of the PC rket this fall, up from 7.9% at lyear, figures New York-based re-rcher Link/IDC. Apple execs see the re improvement as critical, maintain-that software developers—and then tomers—will abandon the Mac if it es more ground to PC als. But to make its rket-share gains, Ap-sacrificed profitabili-—and its long-held et that consumers willing to pay a pre-um for its computers. cent price cuts nar-ed the gap between cs and PCs from 000-plus in 1994 to 0, IDC figures.

Apple isn't giving up its strategy. It recently sweetened discounts to big resellers with $20 million worth of Mac sales a year. And dealers say Apple will cut prices 10% again in January on some PowerBook laptops and high-end 9500 Power Macs. But outsiders worry that Apple can't afford its crusade. Analysts figure Apple's cash balance is down to $200 million. Standard & Poor's and Moody's Investor Services started reviews of Apple's credit on Dec. 18.

That makes internal cost-cutting crucial. Insiders say between 1,000 and 2,000 employees—7% to 15% of the workforce—could be let go before quarterly results come out on Jan. 17. More manufacturing also may be outsourced, and nascent businesses—such as multimedia set-top boxes—may be sold or axed.

Some outsiders contend even that won't do it. Glazer says slashing 1,500 jobs translates into $100 million in yearly savings, vs the $450 million he thinks Apple needs to reach Compaq Computer Corp.'s 23.5% gross margins and earn its 10% net. To fuel development of the Mac alone, Apple spends about 5.6% of sales on R&D, vs. 1.8% for Compaq.

Spindler engineered Apple out of a similar crisis in 1993, when he laid off 13% of the workforce and took a one-time quarterly loss of $188 million. Can he do it again? With gross margins way down, he has less room to maneuver. Thanks to a bloody price war started by Fujitsu Ltd., Apple's Japanese unit, normally the source of 30% of the company's profits, will be lucky to break even this quarter, analysts in Japan say.

Despite rumors, insiders think it's unlikely Spindler will get the boot at Apple's scheduled board meeting in mid-January. "The board stands behind the statement in October in support of Michael Spindler," says a director.

TROIKA TALES. Apple's troubles, meanwhile, have lowered its share price by 34% since mid-July, to about $32—not far above the company's book value of $23.50. That has made Apple takeover bait. Two new suitors said to be sniffing around: Sun Microsystems and a three-way partnership of Apple co-founder Steve Jobs, who left in 1985; Lawrence Ellison, CEO of software giant Oracle; and Jim Manzi, former chief of Lotus Development, the software company recently taken over by IBM.

Sun execs won't comment on rumors, though Eric E. Schmidt, its chief technology officer, calls Apple "a strong brand." As for the troika? No way, says Jobs: "The rumor ain't true. Though there might be romance in the idea, I'm afraid one can't go home again." The question: How much breathing room does Spindler have left?

By Peter Burrows, with Kathy Rebello, in San Francisco and Steve Brull in Tokyo

PEOPLE

FROM BLUEPRINTS TO GRAND DESIGN

Ex-engineer John Correnti now must recast Nucor

As a young engineer, John D. Correnti built factories for a living. The job kept him moving about as often as a traveling salesman. He built blast furnaces in Ohio, a tire-cord factory in Georgia, a uranium plant in Texas. He was usually hundreds of miles away, he now jokes, by the time any glitches appeared. In 1983, Correnti was finishing up a steel mill in Utah for Nucor Corp. when he got a surprise phone call from Chairman F. Kenneth Iverson ordering him to run the plant. Correnti was stunned. "You didn't tell me I'd have to live with my mistakes," he protested.

Iverson just called Correnti again—and this time he's turning the whole shebang over to him. On Jan. 1, the 48-year-old executive will take over as CEO of the Charlotte (N.C.) minimill giant, which is poised to pass Bethlehem Steel Corp. as the second-biggest steel company in America, trailing only the U.S. Steel Group of USX Corp. The transition shouldn't be bumpy for the compact, silver-templed Correnti: Since 1991, he has been Nucor's chief operating officer. What's more, Iverson is sticking around as chairman. Still, taking over for a CEO who led Nucor to 30 years of strong sales growth and solid profits is daunting. "He's an icon," Correnti says.

BACKUP Correnti, left, will still have the counsel of the savvy Iverson, who is staying on as chairman

JOHN D. CORRENTI

BORN Apr. 1, 1947, Rochester, N.Y.

EDUCATION Clarkson University, BS in civil engineering

CAREER PATH Construction engineer at U.S. Steel; plant manager, COO at Nucor

GOAL To expand Nucor by 15% to 20% a year, which would make it the No. 1 U.S. steelmaker

HOBBIES Skiing, reading Dick Francis mysteries

QUOTE "I just want to keep the train on track, steaming ahead"

ADJUSTMENTS NEEDED. Correnti's promotion comes at a trying time for Nucor. For a decade, it has been the high-flying Wal-Mart of the steel industry, keeping costs down on basic products and passing the savings on to customers. But as imitators spring up, also offering cheap, basic steel, Nucor finds itself under pressure to revamp its product mix and get into higher-margin steels. Meanwhile, it's still struggling with new technology at its iron carbide plant in Trinidad. Worried investors have traded the stock down to about $54, vs. last year's high of $72.

Correnti admits Nucor has some adjusting to do. To compete in premium markets, it must improve product quality. Customers in those markets, such as auto and appliance makers, also dema lots of customized attention, a specia of the integrated steel companies.

Yet Correnti takes over a stron nearly debt-free company. As new ch lengers grapple with startups in Ke tucky and Indiana, Nucor already is e perimenting with making upsca stainless steel and ultrathin gauges its Indiana and Arkansas plants. Ph it's busy building a third flat-rolled st mill, a $500 million behemoth in Sou Carolina. Correnti expects Nucor's sal this year to jump 13%, to $3.35 billio and earnings to top 1994's record $2 million. He's looking for 15% to 20 sales growth for the next five yea Even if Nucor stumbles, it likely w eclipse U.S. Steel as the No. 1 ste maker by the year 2000. "After Sou Carolina, it would just take one mo mill," he says.

FRIEND OF BILL. The question is wheth Nucor under Correnti can stay nimb He says he will keep the 22-pers headquarters sm and continue delega ing great powers the plant manage His job? To overs new projects, stay touch with W Street, and visit t 19 divisions two three times a yea Except for all t flying time—spe reading mystery no els—Nucor's rapid growth rate wo be much of a drain on its CEO, he say "What's the difference between 15 di sions and 30 divisions? It's just a fe more lines on the page."

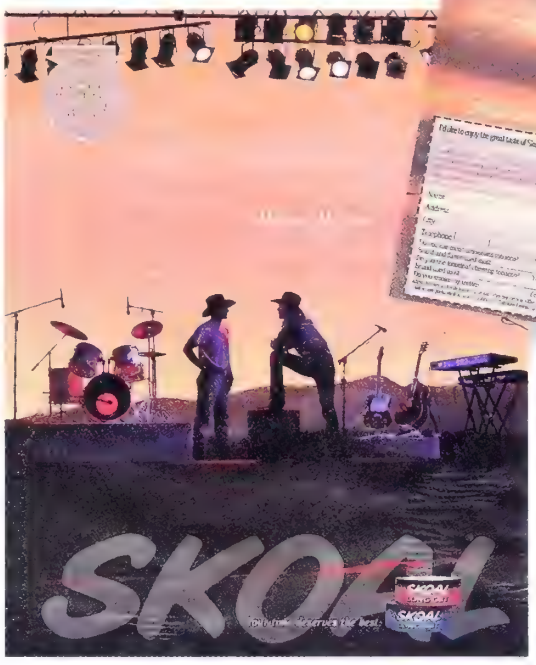
Correnti is regarded as harder-drivi than the genial Iverson, and he preens bit more in the limelight. He ma friends with then-Governor Bill Clint when the company was negotiati plant sites in Arkansas. And he conti ues to meet with Clinton, talking ste and politics at the White House—(more recently, chatting at a Little Ro banquet for retiring Democratic Senat David H. Pryor. "I'm one of the R publican Friends of Bill," he says.

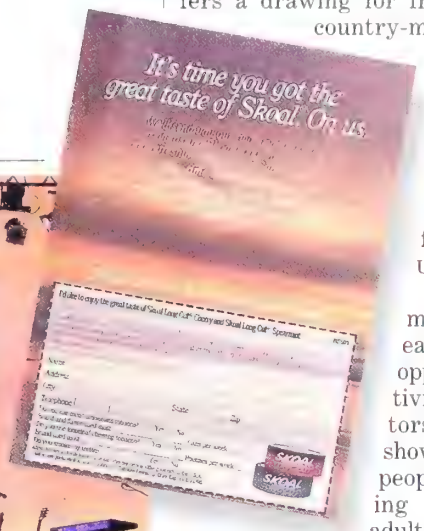
He's also quicker than Iverson make enemies. Speaking at Robert Mo ris College in Pittsburgh, Corren bulled into a subject most executiv sidestep, saying matter-of-factly that would "never dream of building a mil in a union town like Pittsburgh. But competition heats up for Nucor, Co renti's combative ways might be ju what the company needs.

By Stephen Baker in Pittsbur

O SMOKE, UT PLENTY OF HEAT

ny the smokeless tobacco biz is starting to hack





STING
Massachusetts forced tighter rules after it proved minors got free samples from ads in *Rolling Stone*

or years, UST Inc. has chewed up the competition and spit out pure gold. tly because the Greenwich nn.) maker of Skoal and Co- nhagen brand snuffs has ided the political and legal sles that have plagued cigar- e companies, it has posted fit numbers most consumer- ducts outfits can only dream ut. Earnings have doubled five years, to $387 million year—enough to generate efty 32% net margin on $1.2 ion in sales.

Now, UST may be about to chewed up. A study re- ed on Dec. 18 by the Amer- n Health Foundation, a Val- la (N. Y.) organization that ases on research about the lth hazards of tobacco, found t a single can of smokeless acco contains three times dosage of cancer-causing chemicals nd in a pack of cigarettes. (The aver- user of smokeless tobacco consumes ee cans per week.) In Kansas, a m of lawyers is preparing a nation- e class action alleging that UST and ers have known for years that their ducts are addictive and harmful. anwhile, tobacco has until Jan. 2 to pond to Food & Drug Administra- proposals that would sharply curtail keting of smokeless tobacco.

PLE WHAMMY. Perhaps more omi- sly, UST's fundamental business is nging for the worse. Analysts ex- t profits to increase by 11% in 1996, much of the rise will come from her prices. Unit-sales growth for 's smokeless tobacco through the t nine months of this year was a ry 0.5%—after in- ases of 2.6% in 1994 2.3% in 1993 and e those rates in the Os. From about 90% he late 1980s, UST's ket share has fallen bout 84%.

The problem: UST's litional market of tly young blue-col- males isn't expand- Attempts to lure buyers to smoke- less tobacco—mainly former cigarette smokers or younger users—have failed. Competitors, meanwhile, have begun chipping away at UST. Swisher International Inc.'s Helme unit offers its Silver Creek brand in a two-for-one package, while Conwood Co. is selling its new Cougar brand for about half the price of UST's Skoal.

UST is fighting back, but slowly. It recently unveiled Skoal Flavor Packs, a pouch-like version of Skoal designed as an alternative to cigarettes. But similar products have had only limited success with their target market: cigarette smokers. Meanwhile, Joseph R. Taddeo, head of UST's tobacco unit, resigned in June after a dispute with CEO Vincent A. Gierer Jr.—analysts say over the course of new-product initiatives. Taddeo's replacement is marketing executive Robert D. Rothenberg. Gierer, Rothenberg, and other company executives refused interview requests.

Analysts expect Rothenberg to further shift UST's advertising emphasis away from stock-car racing and rodeo audiences to rock concerts and college campuses. Advertising spending is going up, too. One splashy promotion is UST's *Rock The Smokies* campaign, which offers a drawing for free tickets to a country-music concert to be held on Fourth of July weekend in Newport, Tenn. Anyone who sends in a coupon can ask for free samples of UST products.

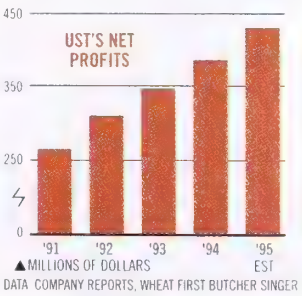
But aggressive marketing could easily ignite more opposition from activists and regulators. "Statistics show that it's young people that start using tobacco, not adults," says Mitchell R. Zeller, a deputy associate commissioner at the FDA. "It's the President's goal that the next generation grow up without becoming addicted to tobacco." The new FDA rules would limit marketing efforts such as sponsorships and the handing out of free samples. The agency also is likely to pressure UST and stores to ensure that they don't sell to minors.

I.D., PLEASE? Some states aren't waiting for Washington. In October, Massachusetts forced UST to consent to stringent restrictions on the use of mail-order samples there, including checking driver's licenses to verify the age of those writing in for samples. This came after a six-month sting in which the state had minors clip coupons in *Rolling Stone* and other magazines, then write for free samples after claiming to be adults. "If you could fill out a coupon and sign something without showing any proof of age and get a six-pack of beer in the mail, people would be outraged," says Assistant Attorney General George Weber.

Diversification would seem prudent at this point. UST got into winemaking in the mid-1980s under the Chateau Ste. Michelle and Columbia Crest labels, but wine still only accounts for 7% of sales and 1.3% of operating profits, hardly enough to offset pressures on its main business. UST may have to come up with something else—or endure some bites into its peerless financial record.

By Tim Smart, with Ed Brown, in New Haven

NO PROFIT PROBLEM



DATA COMPANY REPORTS, WHEAT FIRST BUTCHER SINGER

DEALS

WILL *FLIPPER* PLAY IN ESTONIA?

Why John Kluge is on a buying binge in Hollywood

John W. Kluge didn't get to be one of the richest men in America by being stupid. A onetime Ford assembly-line worker, he invested in a Washington radio station in 1946 and later a string of TV stations. That made his fortune in a big way in 1984, when he sold the TV stations to Rupert Murdoch for $2 billion. He was among the first to jump into cellular, too—picking up a cell-phone operation in 1983, which he sold three years later for a cool $1.6 billion.

Yet for all his lucrative dealmaking, the 81-year-old Kluge has never managed to conquer Hollywood. He has lost an estimated $275 million on Orion Pictures Corp., the production outfit he began investing in during the mid-1980s—only to see it sink into bankruptcy. Orion emerged from Chapter 11 in 1992, but it still gushes red ink. So why would Kluge's Metromedia International Group Inc. swoop in on Dec. 21 to bid $115 million for debt-plagued Samuel Goldwyn Co.? Or, among other apparently oddball deals, agree on Nov. 30 to pay an estimated $533 million for Alliance Entertainment Corp., a distributor of golden-oldie music by the likes of Mel Tormé and Rosemary Clooney? The answer: Eastern Europe.

PICK OF SHOWS. Since the Berlin Wall came down, Kluge and his aides have been aggressively buying up licenses to provide wireless cable TV, radio, and telephones in such places as Riga, Tallinn, and Nizhny Novgorod. Now, Kluge's troops are hustling to line up the programming they intend to sell to these new customers. If it outbids Dutch media giant Polygram for the Samuel Goldwyn studio, Metromedia will gain the rights to a library of 1,100 films, including such classics as *Guys and Dolls* and *Pride of the Yankees*, as well as some 700 episodes of TV programs such as *Flipper* and *Gentle Ben*.

Will they line up in Estonia to see *Flipper*? Hard to say. But Kluge and company certainly think so. In a flurry of deals since August, 1994, Metromedia has also snapped up two smallish film companies. If you add in Orion and Goldwyn, the deals would give Metromedia rights to more than 2,100 films and television shows.

One problem: Much of Kluge's new empire isn't making any money. In a recent filing with the Securities & Exchange Commission, Metromedia acknowledged that its collection of companies lost $51.2 million in the first six months of 1995, on sales of $179.9 million. Moreover, the company is clogged with $399 million in short-term and long-term debt.

Kluge isn't talking about how he intends to turn his money-losers around.

BRAVE FACE: *His new empire is losing mone*

And he shows no sign f altering his strategy. A sociates say Metrome continues to bid for lice es not only in Easte Europe but also in As The company alrea ships such U.S. progra as MTV, Country Mu Television, and the D covery Channel to wi less cable-TV subscribe in such cities as Mosc Bucharest, and Tashke It also owns radio statio in Moscow, Budapest, a elsewhere, and is buildi wireless phone systems other regions.

Looking for financial stability, l April Kluge merged Metromedia wi Actava Group Inc., a mishmash of co panies formerly known as Fuqua Indu tries. Its chairman, John D. Phillips, is 52-year-old turnaround specialist who h sold off everything but Actava's Snapp Power Equipment unit. An executi whose tastes run to denim and Harl Davidsons, Phillips will act as CEO Kluge's entertainment companies fr from Actava's Atlanta headquarters.

As a source of new programmin Kluge is counting on Motion Pictu Corp. of America (MPCA), a producti house he agreed on Nov. 27 buy for $32.5 million in sto and cash. MPCA, which pr duced such low-budget hits *Dumb and Dumber* and *Thre some*, plans to turn out 14 16 films next year for Metr media. If Metromedia wi Goldwyn, which specializes art films such as *The Madne of King George*, it would g ownership of a dozen oth films in the works, includi *American Buffalo* with Du tin Hoffman.

Can a library of movies a some startup production he put Kluge's entertainment b in the black? Possibly. Mo likely, they will keep him in t game long enough to mak back the losses from his Ori debacle—and find another, bi ger company to buy him ou After all, some of John Kluge shrewdest moves have con from knowing when to sell.

By Ronald Grover
Los Angel

KLUGE'S MEDIA EMPIRE

ORION PICTURES Has a film library of 1,200 movies, including *Platoon, Terminator,* and *Silence of the Lambs.* Emerged from bankruptcy in late 1992. Lost $18.9 million on $73 million in revenues for the six months ended Aug. 31.

METROMEDIA INTERNATIONAL Provides wireless cable TV, paging, and telephone services to Eastern Europe and former Soviet-bloc nations. Lost $13.1 million on $3.3 million in sales for the first six months of fiscal 1996.

SAMUEL GOLDWYN* Owns a 52-theater chain and a library of 1,100 films, including *Pride of the Yankees* and *Guys and Dolls,* and 700 TV episodes. It also has film production and distribution. Lost $12.3 million on sales of $53.5 million in the six months ended Sept. 30.

*Bid to acquire company on Dec. 21

DATA: COMPANY REPORTS

GOLDWYN'S *THE MADNESS OF KING GEORGE*

Purina Mills Satisfies Data-Hungry Decision Makers with the SAS® System

Every business day, information managers at Purina Mills— America's leader in animal nutrition—satisfy a different kind of craving: the need of top executives to get their hands on strategic information to support better quality decisions.

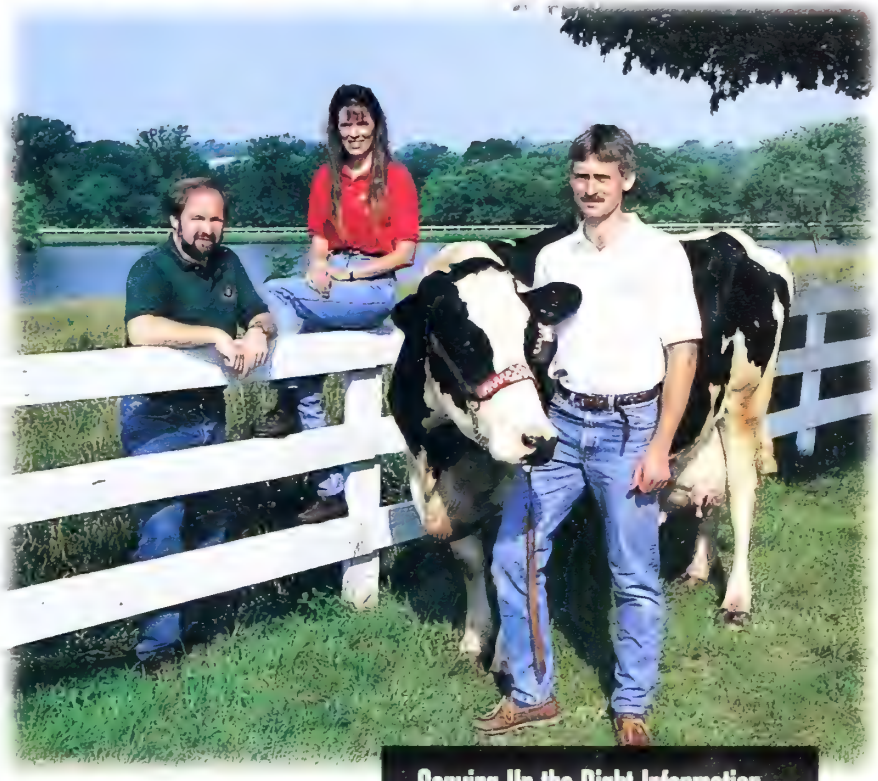
Luckily, they've cut preparation time substantially since adding SAS software to their menu of productivity tools. "Comparing the SAS System to anything else we've ever used to analyze business data, I'd say SAS software is by far the best," says Gerry Daignault, Region Controller. "There was a time when we had to do things manually. But today, we can review many aspects of our business just by pointing and clicking."

Purina Mills relied on the SAS System to build client/server applications now in use by field representatives and managers at specific manufacturing locations. Daignault adds that "SAS software is so simple to use that even those managers and executives who have not previously used computers feel right at home."

Speeding Decisions at Every Level

According to Mike Durbin, Supervisor of Information Services for Purina Mills, his department needs to get information to managers as quickly as possible, who in turn must deliver relevant details to upper management as quickly as possible.

"We use SAS software in many areas of operation including budgeting, research, and as a management support tool," says Durbin. "Activities include tracking customer volume, current income, and comparative analyses of income year-by-year."



Daignault, Brown, Durbin

Serving Up the Right Information... at the Right Time

Connie Brown, Purina Mills Information Analyst, says the key business benefits of using the SAS System are "improved productivity by key field management and a consistent thought process in the use of management information. There is no question that field management spends less time gathering numbers and more time using good information to support the decision process. Mapping and graphical presentations are becoming more important in the decision process, and SAS Institute has been very supportive in helping us implement these tools."

"SAS software is doing the job for us," Daignault concludes. "All of our directors will eventually have it available."

To receive a SAS System Executive Summary, give us a call or send us E-mail at bw@sas.sas.com

The SAS System

Executive Summary

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CORPORATE GIVING

THE NAACP BETS ON A NEW BREADWINNER

Kweisi Mfume hopes to show donors the crisis is over

Last March, officials of the scandal-plagued National Association for the Advancement of Colored People asked members of the AT&T Foundation to lunch at Manhattan's Remi restaurant. Myrlie Evers-Williams, who had just taken over as NAACP chair, quickly got down to business. What could the nation's venerable civil rights organization do to persuade the foundation to renew a three-year, $225,000 education grant that had expired in 1993? AT&T's answer: Put your house in order. "We were looking for strong leadership, strong financial controls, and a strong mission," recalls Milton J. Little, an AT&T Foundation vice-president who was at the meeting.

Enter Representative Kweisi Mfume (D-Md.). On Feb. 15, Mfume will leave Congress to become president and CEO of the NAACP, a move that figures to bolster its clout—and its bottom line. Already, his appointment may have won over one big donor: On Dec. 28, Nissan Motor Corp. USA is expected to announce it will donate $100,000 to the NAACP. The organization's backers hope others will follow. "We wanted someone whose integrity was first-rate," says Nancy L. Lane, director of corporate affairs for Johnson & Johnson, who served on the NAACP's search committee.

DAUNTING TASK. Mfume's challenges are twofold: He must attract young blacks now drawn to militant leaders like Louis Farrakhan while reassuring Corporate America that the NAACP is worthy of support. "We need to change the hearts, minds, and direction of young people so that they see appreciation of work, respect for elders, and individual responsibility as bedrock principles," he says.

Mfume thinks this message of self-reliance will appeal to donors. "I hope corporate partners who have not shied away will say to others that it's all right to come home to the NAACP," he says. The task is daunting. The 87-year-old organization has been reeling since August, 1994, when it ousted Executive Director Benjamin F. Chavis Jr. after discovering he had paid $300,000 to settle a sexual-harassment suit. Auditors found other evidence of gross financial mismanagement. The scandal led to longtime Chairman William F. Gibson's defeat last February to Evers-Williams.

IDEA BROKER: *Mfume was an effective Capitol Hill mediator*

Mfume is meeting with auditors to come up with fiscal controls for the group, which is $3.8 million in debt. He hopes to build a $150 million endowment by 2001, improve efficiencies by merging regional offices, and ask some suppliers to restructure or forgive debt.

Business, which contributed almost half of the NAACP's 1995 budget of $8.5 million, is key to his efforts. Despite financial disarray, many companies, including Procter & Gamble, Sears, Quaker Oats, and IBM, have kept up support. Companies argue that business has an interest in backing groups that promote minority opportunities. "It's important we have a skilled and qualified workforce," says Eric R. Graves, manager of constituency affairs at Texaco Inc.

Other corporate donors couldn't ignore the disorder. In 1995, corporate giving declined some 30% from 1994. Joseph E. Seagram & Sons Inc. withhe its annual $50,000 grant in 1994 and 19 Seagram spokeswoman Patsy Glazer sa the company had been waiting to s who would head the organization. No she wants to meet with Mfume. Mer Lynch & Co. also is withholding suppo until it sees how the NAACP's game pl shapes up. AT&T is waiting, too, but Lit is hopeful: "We believe Mr. Mfume's lea ership is what is needed."

SALES TOUR. Backers say Mfume prov his leadership mettle as a member the House Banking Committee. The he emerged as a consensus-builder, m diating disputes among the banking, i surance, and securities industries. Sa Banking Committee Chairman Jam A. Leach (R-Iowa): "There are so people who think that what's good f the free market is bad for lower-incom people. Kweisi believes the reverse-that what makes the market work w be better for lower-income people."

That philosophy is behind Mfume plans to set up NAACP mentoring pr grams to match students with corp rate volunteers. He also wants to wo with companies to set up apprentic ship programs and with officials to in prove public schools. He may also pus for incentives to encourage corporatio to work with small minority companie

Over the next few weeks, Mfume i tends to embark on a nationwide tour t meet with corporate leaders. But wit the NAACP's programs barely functionin many branch offices virtually close and one-third of its staff on furlough the organization could be a tough sell. I will take all of Mfume's skills as bridg builder to convince Corporate Americ that the NAACP won't be just anothe bad investment on corporate books.

By Susan B. Garlan in Washingto

WHERE THE MONEY GOES

NAACP programs that draw corporate support

FAIR SHARE Helps corporations set and reach goals regarding minority hiring and purchasing from minority suppliers

ACT-SO Nationwide competition among students on academic subjects such as arts, humanities, and sciences

BACK-TO-SCHOOL Encourages dropouts and troubled students to continue their education by providing tutoring and counseling

ARKETING

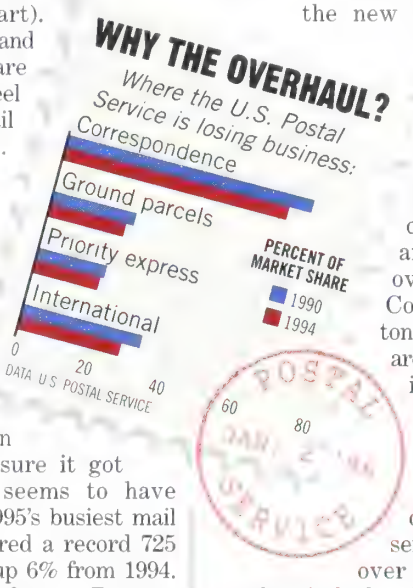
EPACKAGING HE POST OFFICE

acilities are getting face-lifts, erks are getting friendlier

When retired CIA analyst William R. Dodge stopped at Furr's supermarket in Albuquerque on ec. 22, his shopping list included but-; chocolate chips, nuts, and postage mps. Stamps? Sure. Overnight deliv-, too. The Albuquerque facility is one eight that the U.S. Postal Service ently has tucked inside popular retail tlets around the country.

The new offices are just one sign that e USPS is trying to reinvent itself. ide from opening facilities in outlets h as Furr's and Kmart, it is sprucing old offices and improving customer vice. Stamps—including new, self-adsive ones—can now be purchased at Ms, by phone, and with credit cards. ring the holidays, sales clerks direct-traffic and branch hours were exded. Workers even dressed as Santa deliver Express Mail.

Why the changes? After all, the agenis flush from last year's rate hike, higher mail volume, and better cost controls and cash management. Postmaster General Marvin T. Runyon says he ended fiscal 1995 with a record surplus of $1.77 billion on revenue of $54.3 billion. But in many markets, the Postal Service is losing out to private carriers and new technologies such as fax machines (chart). "We just can't sit here and say to people, 'Here are our hours and, if you feel like it, bring your mail to us,'" says Runyon. "We need to get [market share] back."



The new approach was evident over the holidays. Runyon hired 40,000 part-time workers to sort mail, leased 116 planes to carry it, and set up a command center in Washington to make sure it got through. The effort seems to have worked: On Dec. 20, 1995's busiest mail day, the service delivered a record 725 million pieces of mail, up 6% from 1994.

To publicize the reforms, Runyon hiked his ad budget 50% in 1995, to $143 million. Last fall, he also hired Loren E. Smith, a former Citibank executive who did stints at Kraft General Foods Inc. and Colgate-Palmolive Co., to oversee marketing.

At the heart of the new strategy are the new postal "stores." So far, 200 of the 40,000 local offices have had face-lifts that include attractive lighting and salesclerks trained to be friendly and helpful. It's looking good: On average, the new shops have posted 20% sales gains over the offices they replaced. Now, Smith is stepping up the pace—all postal facilities in Albuquerque and Atlanta are getting make-overs. Philadelphia; Columbus, Ohio; Boston; and Richmond, Va., are next. New services include phone debit cards and a "Pack-and-Send" wrapping service.

Shoppers who endured surly postal service and long lines over the holidays likely are skeptical of such reforms. But Runyon knows he has to make the strategy work—or see a lot less mail with a USPS postmark.

By Mark Lewyn in Washington

EOPLE

HE IS HE NRA

s first female chief is out to ist Clinton and lure women

Marion P. Hammer was working late one night in Tallahassee when a carload of thugs followed her into parking garage and threatened her. reached into my purse, pulled out gun, brought it up through the dlights, and aimed right at the driv-' she recalls. "He put it in reverse, tires started smoking, and y were gone."

That was a decade ago, when mmer was lobbying the Flori legislature to relax restrictions handguns. Her success there ped kick off a 28-state move-nt to ease restrictions on car-ng concealed weapons. In De-aber, her record as a winning byist and hard-line opponent gun control helped her become first female president of the million-member National Rifle Assn. after her predecessor, Thomas L. Washington, died of a heart attack. Hammer, who had been vice-president, is expected to run unopposed in April for a one-year term of her own.

Now, the 56-year-old Hammer has her adversaries firmly in her sights. She wants Congress to overturn the federal assault weapons ban. "Restrictions on gun ownership are just a form of harassment," she says. Next up is the defeat of pro-gun-control politicians—starting with the President. "The one thing we definitely plan to do is to work to beat Bill Clinton," says Hammer.

Hammer's confrontational style may be just right for today's embattled NRA, which has image and money problems, has recently lost 200,000 members, and is being audited by the Internal Revenue Service for allegedly commingling funds. To boost membership again, Hammer plans to step up the NRA's appeal to women and families using two time-honored NRA programs: the "Refuse to be a Victim" educational campaign for women, emphasizing crime prevention and self-defense while promoting gun ownership; and the "Eddie Eagle" gun-safety campaign for children, which is Hammer's personal creation.

TRUE BELIEVER
Lobbyist Hammer fended off thugs with a hidden weapon, then sparked a 28-state push to ease curbs on handguns

"WILDLY SUCCESSFUL." Under Hammer, the NRA won't neglect politics at the statehouse either. She spent 20 years lobbying in Florida on behalf of gun owners and proudly points to Florida's first concealed-weapons permit, which allows her to pack her .38 caliber Colt Detective Special or her 9-mm Beretta semiautomatic. "During the past three years, the NRA has been wildly successful in the states, and Hammer is the poster child for the conceal-and-carry issue," laments Josh Sugarmann, director of the Violence Policy Center, a gun-control group.

Hammer, a grandmother of three, likes to unwind at the target range after a day of hard lobbying. On the range or at the office, her opponents say, she seldom misses her mark.

By Paul Magnusson in Washington

HEALTH CARE

NEWBORN BABIES, BAWLING MOMS

They want laws to make insurers pay for longer hospital stays

It is likely the most reviled fiat in recent medical history: 24 hours after childbirth, mother and baby are out the hospital door, cut off by their insurer. "So negligent," says Kathy Sargent, an expectant mother in Westport, Conn. "Appalling," says Randi Curran of San Francisco, who will give birth this spring. "It must be men who made up this policy."

Managed care has met the masses—and the masses aren't happy. Perhaps 40% of newborns currently are discharged after one day, say hospitals, twice the number in 1990. The economics driving that shrinkage are compelling: Childbirth is by far the most common reason Americans enter hospitals, and reducing stays would save insurers hundreds of millions of dollars a year. Most mothers, though, would rather stay put, and doctors don't want medical decisions taken out of their hands. The result is "a rallying point for people who have bad feelings about managed care," says Michael A. Maffetone, CEO of University Hospital at Stony Brook, N. Y.

STATEHOUSE ACTION. The outrage has found an outlet: In 1996, 25 states are expected to introduce legislation that would require insurers to pay for a 48-hour inpatient stay for normal deliveries when a physician prescribes it. Five already have passed such laws. In California, where health-maintenance organizations pioneered the one-day stay years ago, insurer pressure to reduce postpartum stays to 12 hours has legislators promising a bill on Governor Pete Wilson's desk in January. Senator Bill Bradley (D-N. J.) is amassing support for similar federal legislation.

In this debate, pure medicine may be on the insurers' side. While some doctors and hospitals say they're seeing more cases of jaundice and dehydration in newborns, the hospital readmission rate for babies remains around its traditional 2%. Several studies have found no link between one-day stays and consequent complications. "There is virtually no clinical evidence that there's a technical medical necessity for an acute medical stay of more than 24 hours," says A. Bruce Campbell, chief medical officer at Aetna Health Plans.

Insurers and HMOs have joined with the U. S. Chamber of Commerce and groups such as the American College of Nurse-Midwives to battle mini-

MUCH ADO?

Shorter initial hospital stays for newborns haven't led to a higher readmission rate

mum-stay legislati
Many hospitals, t
worry that gove
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simply will force
surers to cut compensation elsewher

Some hospitals have devised an
ternative solution: A growing numb
are offering to absorb the cost of a s
ond night's stay for mothers whose
surers don't pay. Hospital executiv
say they're motivated primarily by sa
ty concerns, but they admit the atter
ing publicity doesn't hurt. "I will r
lie," says T. J. Padden, administrator
Box Butte General Hospital, a 44-b
facility in rural Alliance, Neb. "It's no
bad marketing thing." Incremental co
for additional nights are low—rare
more than $200 a night, and far lower
Box Butte. Stony Brook, the first hos
tal to underwrite longer stays, says
maternity admissions are up 8% in t
past six months.

FLAT FEES? The downside to this a
proach, say other hospital executive
is that it ultimately could weaken the
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ing the cost on one procedure could e
courage HMOs to cut back on other
For now, though, the commotion m
be gaining the desired effect. Hospita
that pay for a second night say some i
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Ultimately, managed care likely w
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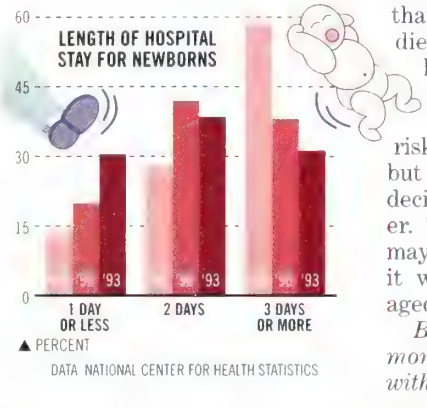
*By Keith H. Han
monds in New Yor
with bureau reports*

BABIES OUT THE DOOR



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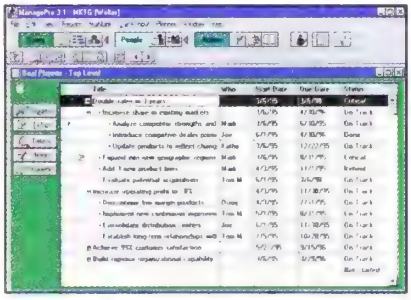

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The National Arbor Day Foundation

RESEARCH

A HEAVYWEIGHT CONTENDER

This breakthrough may be th key to a fat pill

Last July, Amgen Inc. looked like had a lock on one of the drug dustry's most heated races: t search for a "fat drug." In a much-he alded study whose announcement boo ed Amgen's stock by $900 million, searchers disclosed that a protein call leptin, produced by the newly disco ered OB gene, stripped away body f when injected into obese mice.

Barely five months later, an Amg rival may have taken the lead: On De 28, Millennium Pharmaceuticals Inc. Cambridge, Mass., was to announce th it had found the "receptor" for leptin the structure on cell walls that is a cr cial part of regulating leptin's functio Receptors don't make anyone skinn but many drugs target receptors to i hibit or stimulate a bodily functio While Amgen is testing an injectab drug, Millennium says its receptor ma be the key to an antiobesity pill, whi would be far more lucrative.

MIND-SET. Researchers had hoped shortage of leptin—the protein that si nals the brain to stop eating—was big factor in obesity. But studies no show that obese people often have hig leptin levels. Millennium believes th receptor it found will lead it to anoth obesity gene, called DB, that determin whether the brain can recognize leptin stop-eating signal. "The receptor ma lead to drugs for potentially the mo prevalent form of human obesity—o resulting from the brain's resistance leptin rather than the lack of leptin says Millennium CEO Mark Levin.

Weight-watchers shouldn't rethin New Year's resolutions yet: Researche say a wonder drug is years away.

By Geoffrey Smith in Bosto

DITED BY THANE PETERSON

TRUNKFUL OF PINK LIPS AT BUDGET

ITH THE RENTAL CAR BUSIss wrapping up one of its orst years ever, Budget ent a Car's new chairman, ck Frazee, had a Grinchke holiday message for 500 laried employees: Your serces are no longer needed. razee hopes to save $20 miln annually by cutting 20% the salaried workforce. The ts are part of a massive akeup at Budget, the No. 3 ntal agency with estimat- 1995 U.S. revenues of $1.5 lion. Frazee also showed e door to his CFO and two nior vice-presidents and sed 40 unprofitable offices. anding out pink slips over e holidays was "not fun," razee says. "But I try to remind the people who are left that the company is a lot more stable as a result of the actions we've taken."

CLOSING BELL

THE JOBS MARKET

ood thing Steve Jobs knows ne ups and downs of entreeneurship. His company, ixar Animation Studios, aker of *Toy Story*, went ublic on Nov. 29, sending ne stock to 39. Then Pixar ell to 23 on worries that ne bulk of *Toy Story*'s earnigs will go to partner Walt isney. But just after Christas, Pixar shares edged ack up, to $28, after sever- analysts rated the stock "buy." The current value f Jobs's 80% stake: $840 illion.

DATA: BLOOMBERG FINANCIAL MARKETS

PIER 1'S $20 MILLION QUESTION

PIER 1 IMPORTS ALSO HAD A lump of coal in its Christmas stocking: The retailer disclosed on Dec. 26 that it would post a pretax loss of $20 million because of "inappropriate trading activities" by a financial consultant—Capital Insight of Beverly Hills, according to the consultant's lawyer—hired to manage excess cash and short-term investments. Pier 1, otherwise enjoying strong sales gains, says the loss won't materially affect liquidity or operations, but a board committee is investigating. Pier 1 CEO Clark Johnson didn't return phone calls.

IS CYRIX LOOKING AT A DEFAULT?

CHIPMAKER CYRIX IS SPUTtering. On Dec. 22, the company warned that it may lose $8 million or more in the fourth quarter. A price collapse forced Cyrix to write down its inventory of chips compatible with Intel's 486. Cyrix said the loss could force a default on $88 million in loans used to purchase production equipment to build its newest chip, which is designed to rival Intel's new Pentium Pro. The company hopes to get a waiver from creditor IBM, which manufactures Cyrix' newest chip.

A DESERT DEAL FOR BRITISH PETROLEUM

DESPITE A BLOODY INSURgency by Islamic militants in Algeria, British Petroleum on Dec. 23 signed a five-year deal with Sonatrach, Algeria's state-owned oil company, to explore and develop gas fields in the remote I-n-Salah region of the Sahara desert. BP will foot 65% of the $3.5 billion cost of the project and will get one-third of the gas's sales value—enough, it figures, to boost its worldwide gas production by up to 30%. A spokesman says BP is hoping that energy installations, which account for 95% of Algeria's foreign earnings, won't be targeted by the insurgents. Exxon and Atlantic Richfield also are mulling deals in Algeria.

HEADLINER: WHITNEY HOUSTON

EXHALE BLOWS 'EM AWAY

Call it a Christmas miracle. No one was more surprised than execs at Twentieth Century Fox when its *Waiting to Exhale* opened on Dec. 22 and immediately became the unexpected hit of the holidays. Fox had targeted its marketing for the film, starring singer Whitney Houston and three other black actresses, heavily at black women. Exhale opened primarily in large cities; the studio hardly even opened the movie in the 'burbs until after Christmas.

Hollywood isn't sure why, but despite its segmented marketing and limited distribution, *Exhale* is knocking 'em dead. The film, based on a novel by Terry McMillan, was made on a budget of $15 million, about half the Hollywood average. In its opening weekend, the movie had a huge $14.3 million box office, beating out six other new films, including Warner Bros.' *Grumpier Old Men* and Universal Pictures' *Sudden Death*. Being one of the few women-oriented films helped. Whatever other reasons for *Exhale*'s success, Hollywood won't ignore the lesson: Look for a wave of black-female buddy movies—glitzier, big-budget ones.

By Ronald Grover

CALLING CORPORATE AMERICA'S BLUFF

IN THE MAYBE-IT-DOESN'T-PAY to-stick-your-neck-out category: House Minority Leader Richard A. Gephardt and 45 fellow Democrats are challenging more than 90 executives to detail business tax breaks they would be willing to sacrifice to help balance the federal budget. The challenge, in letters mailed Dec. 22, was prompted by national newspaper ads signed by the business leaders imploring Congress to put "everything on the table" to reach a budget deal. Among others, the letter went to Paul Allaire of Xerox, Lou Gerstner of IBM, Bob Allen of AT&T, and Joe Dionne of The McGraw-Hill Companies, parent of BUSINESS WEEK.

ET CETERA . . .

- The Feds and Occidental Chemical settled the 16-year-old Love Canal cleanup case.
- Cordis shares fell after Johnson & Johnson extended its review of its buyout offer.
- Daiwa's ex-N. Y. general manager was indicted for allegedly helping hide losses.
- Goldman Sachs is mulling whether to dissolve its partnership and go public.

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DITED BY DOUGLAS HARBRECHT

RTHUR LEVITT SPEAKS SOFTLY ND CARRIES A LITTLE STICK

When President Clinton unexpectedly vetoed a securities-litigation reform bill on Dec. 19, it marked a setback for Securities & Exchange Commission Chairman thur Levitt Jr. The SEC chief had toiled for months to ge a compromise that satisfied Republicans' desire to curb isance suits and the Administration's insistence on pro-tion for small investors. Congress overrode the veto, but debacle dealt a blow to Levitt's dream of becoming a con-nsus-builder able to bridge the gulf on Capitol Hill.

Because the veto blindsided GOP law-kers, Levitt comes off looking ineff-tual. White House pols seeking fa- with the trial lawyers' lobby swayed President, rather than Levitt. And vitt's O.K. of a "safe-harbor" section the bill that protects companies from ts over false projections riled con-ner groups. "Levitt's credibility has en deeply wounded by playing poli-s," says Michael A. Calabrese, a di-tor of Congress Watch and an oppo-nt of the bill.

VETO: *It makes him look ineffectual*

PLAYER? Levitt, 64, former chair-n of the American Stock Exchange, was viewed as a vy regulator when Clinton appointed him in 1993. Since Republican takeover of Congress, he has skillfully court-GOP legislators. His modus operandi: seizing chances to get h the Republicans' deregulatory program. For example, af- winning GOP concessions on the safe-harbor provision of securities-reform measure—including the exclusion of h protection for initial public offerings—Levitt signed off that portion of the bill. High-tech companies with volatile ck prices had sought the change to reduce their expo-e to costly lawsuits.

While Levitt contends he would have opposed the legisla-n if the safe-harbor provision had not been modified, critics mble that he chose to blink rather than duke it out with Republicans. "I was stunned," says former SEC Commissioner Richard Y. Roberts, a Republican, of Levitt's position.

More surprising, though, was Levitt's nonrole in the President's veto decision. Clinton relied mainly on longtime Arkansas adviser Bruce Lindsey and Deputy Chief of Staff Harold Ickes in arriving at his no-go decision. Levitt, for his part, insists his views were well known to the White House.

The perception that Levitt was a bit player in the affair could hurt next year when the House will consider paring back securities regulations. Rather than mounting an all-out assault on the bill's objectionable provisions, the SEC chief is trying to win a place at the negotiating table while pushing to eliminate overlapping state and federal regulations. Yet with Levitt's White House clout now in question, the bill's sponsors may be less inclined to make concessions.

Levitt's efforts to protect his agency's funding could also take a hit. So far, his accommodating approach has paid off. Republicans who have savaged other regulatory agencies are expected to hold the SEC budget steady at $300 million in 1996. But Congress could well make another run at the regulator's budget next year, while Levitt appears weakened.

Despite his recent wounding, Levitt shows no signs of a retreat from his agenda. He still intends to pressure the National Association of Securities Dealers to reform the NASDAQ market and make it more equitable for small investors. And the SEC chief is about to unveil a proposal to require more disclosure of derivative holdings, which could greatly complicate companies' public filings. "I expect flak from all quarters," Levitt says serenely. But his success in dodging the next round of artillery shells may determine the legacy Levitt leaves behind at an embattled SEC.

By Amy Barrett, with Michael Schroeder

CAPITAL WRAPUP

HAT'S BUGGING THE FEDS

It seemed like farce to many for-gners, but it's no laughing matter at ie Central Intelligence Agency and ie Federal Bureau of Investigation. oth agencies have launched probes find the source of press reports last ll that the CIA snooped on the phone lls of Japanese officials during .S.-Japan auto trade talks. And ey're aiming high: They inter-ewed Deputy Treasury Secretary awrence H. Summers and other eco-mic officials. Summers, who says he played no role in the auto talks, denied involvement. The CIA no longer considers him a suspect, but investigation continues.

BALKANIZED AID PACKAGE

▶ Bringing peace to Bosnia may be easier than getting Congress to O. K. $600 million in reconstruction aid. The Clintonites will sell it as a U. S. job creator. But there's a hitch: The White House wants to divert some work to the Eastern European countries hurt most by a trade embargo against Serbia. The Hill may balk at that.

BUDGET SLOW BOAT

▶ Protracted wrangling over the fiscal 1996 budget has dashed any chance that President Clinton will send Congress a fiscal 1997 budget by Feb. 5, the statutory deadline. After two government shutdowns and marathon budget talks, the Office of Management & Budget is two months behind in its review of agency spending proposals for the next fiscal year. The most likely outcome: The White House may send just a letter to Congress explaining the delay.

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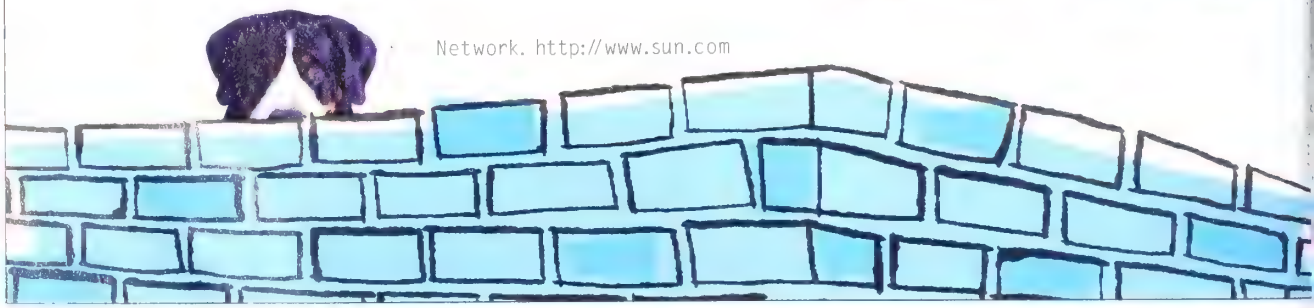


DITED BY STANLEY REED

JAPAN'S SHADOW KINGMAKER S BIDDING FOR THE SPOTLIGHT

chiro Ozawa has always preferred the role of shadow king-maker in Japanese politics. Back in 1993, the brash politi-cal heavyweight helped lead a mass defection from the en ruling Liberal Democratic Party, snapping its 38-year ign. When his reformist government collapsed in 1994, awa pulled off an improbable merger of nine parties into an position bloc called the New Frontier Party but didn't ke the top leadership post.

Now, Ozawa, 53, has emerged from the shadows. In mid-ecember, he announced a surprise bid to challenge longtime leaguе Tsutomu Hata to lead New Fron-r. And when the results were tallied on c. 27, Ozawa won by more than 2 to 1. The ge is now set for an epic battle between awa and LDP President and International ade & Industry Minister Ryutaro Hashimo-in a general election sometime in 1996. At ke will be control of the Diet's 511-seat ver house and the Prime Minister's chair.

S VAGUE AS POSSIBLE." Ozawa's bid for the otlight is timely. After four years of eco-nic stagnation and a string of bank fail-es, the Japanese public is fed up with the cialist-LDP government's dysfunctional man-ement of the economy. Socialist Prime Min-er Tomiichi Murayama's coalition is coming der withering attack for a plan to use $6.6 billion in public ney to bail out seven insolvent housing-loan corporations, ich made reckless real estate loans in the 1980s. "The in-t is to be as vague as possible about the assignment of me," Ozawa told BUSINESS WEEK. "This is the kind of soci-Japan has become."

Ozawa wants to remake the Japanese system. He cham-ns sweeping deregulation. He also wants to give the now ak Prime Minister's office enough power to set clear poli-directions. Japan's glacial consensus-style decision-mak-threatens to consign the nation to decline, he warns. "No leader has come up with a strong vision of how to go forward," he says.

Ozawa's biggest liability aside from heart problems is his association with the money politics he says he wants to clean up. After all, he was a key LDP fund-raiser and power broker for years. He is taking heat right now for his ties to a Buddhist organization that turned out 6 million votes to support Ozawa candidates in last July's Upper House elections. Ozawa's rise could also bust up New Frontier if he can't keep Hata on board.

OZAWA: *The next Premier?*

Hashimoto, who made a big splash by staring down Washington in last summer's auto talks, is much more popular than Ozawa. Still, there is growing sentiment in Japan that Ozawa may be the only leader who can produce significant change. "He's very determined, and the time left for Japan to pull out of this stagnation is limited," figures Masaya Miyoshi, president of the Japan Federation of Economic Organizations, or Keidanren.

Indeed, Ozawa has won plaudits from some economists for his proposal to halve income and corporate taxes, wipe out special-interest loopholes, and eventually make up some of the difference by hiking Japan's sales tax from 3% to 10%. But with Japan's budget deficit projected to hit 4.2% of gross domestic product in 1996, vs. 2.0% in the U.S., Ozawa has to be careful not to lead Japan into a fiscal mess.

Ozawa could also help heal strained ties with the U.S. He is a pragmatist on trade who is well regarded in Washington. Ozawa says he is worried that Washington has started to lose interest in Japan. He finds it regrettable that there is a tendency in Washington "to treat the U.S.-Japan alliance more lightly than before." If Ozawa becomes Prime Minister, that would certainly command American attention.

By Brian Bremner in Tokyo

GLOBAL WRAPUP

RIVATIZING A BRAZILIAN GIANT

Brazil's slow-moving free-market re-rms are getting a fresh impetus from ıe sale of Companhía Vale do Rio oce, the state-controlled mining gi-ıt. In what's likely to be Latin Amer-a's biggest privatization, Brazil on ec. 20 picked a group headed by Mer-ll Lynch & Co. and Rothschild Inc. om a star-studded field of competi-ırs to manage the sale of the govern-ent's 51% share in CVRD. The sale, ·t for late 1996, should fatten state ıffers by at least $5 billion.

Privatization of CVRD will mark "the point of no return" for Brazil's move away from decades of statism, says Amaury Bier, chief economist of Citibank in São Paulo. Recently, investors had been growing uneasy over the slow pace of free-market legislation in Brazil's Congress. The naming of the sale managers shows the government "is serious about moving ahead," says Ricardo Gallo, vice-president for capital markets at Bank of Boston in São Paulo.

The Merrill Lynch group will earn a 1.9% commission on CVRD's sale price. The lucrative job drew bids from such heavyweights as Citibank, J.P. Morgan, and Salomon Brothers. A key issue is whether to sell the government's shares in a global public offering or auction off operations such as mining, forestry, and transport separately. But the choice of Merrill Lynch, which joined with CS First Boston to manage a $3 billion stock sale of Argentine oil company YPF in 1993, indicates that Brazil favors privatizing CVRD through a similar high-profile public offering.

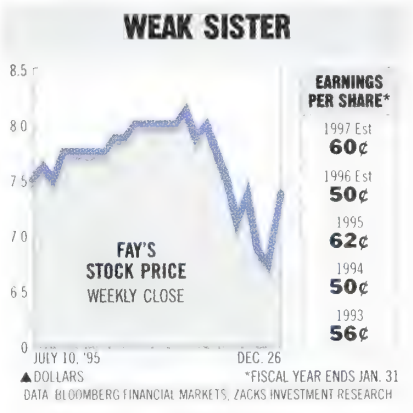
By Ian Katz in São Paulo

BY GENE G. MARCIAL

FAY'S DRUGS: FIT TO BE SWALLOWED?

The "shakeout" investors—who buy into companies whose industries are in the throes of consolidation—are convinced that Fay's (FAY), the nation's 13th-largest drugstore chain, is ripe for picking. The shares have dropped to 7, down from 9¾ in late April, partly because of investors' disappointment that a rumored takeover has not yet materialized. And a flurry of yearend tax-loss sell-offs may be adding to the downward pressure.

But the focus, insists one big investor, should be on what's happening to all drug chains. "A shakeout in the industry is under way," notes analyst



Maurice Levenson of Value Line. This is being fostered, he explains, by the emergence of managed-health-care plans and stiff competition from giant discounters such as Wal-Mart Stores and Target Stores. Analysts note the industry could also shed a lot of duplication and costs by buyouts of weaker companies. A recent example is Rite Aid's agreement to acquire Revco for $1.8 billion.

Fay's—with its sales sluggish, its earnings down, and the stock on the ropes—is regarded as one of the industry's weak sisters. "It's similar to the Revco situation. The likes of such possible suitors as Walgreen's could swallow it up just like that," says investment manager Mike Kicera of MRK Capital Management.

Kicera figures that Fay's shares are worth 12 to 15 in a buyout—based on what Rite Aid agreed to pay for Revco. With 276 outlets in New Hampshire, New York, Pennsylvania, and Vermont, Fay's is streamlining its operations by getting rid of noncore businesses. It sold off Wheels Discount Auto Supply Div. to Sears Roebuck's Western Auto Supply for $37 million. Management is also expected to unload the 30 Paper Cutter discount-office-supply stores.

"Without Wheels and Paper Cutter, Fay's would be a much more attractive takeover target," says one money manager accumulating shares.

Providing added inducement for Fay's to sell: Management and directors own about 31% of the stock—including the holdings of the family of Chairman Henry Panasci Jr. Fay's didn't return calls.

THE WAY THE OLD RUBBER CRUMBLES

Not everything in today's hot IPO market is Internet-related. One issue that some pros like—GreenMan Technologies (GMTI)—is nowhere near cyberspace: It's in tire recycling. GreenMan went public on Oct. 3 at 5 a share. On opening day, the stock jumped to more than 8 and stayed there for eight trading days—until profit-taking spoiled some of the fun. But some money managers still think it's worth loading up on GreenMan—now at 6.

What's the allure of tire recycling? GreenMan uses a patented cryogenic (low-temperature) technology to make used tires brittle, thus yielding crumb-rubber granules. These granules are a low-cost source of rubber and plastic waste, according to one money manager who has a sizable stake. GreenMan's chief product is a proprietary thermoplastic rubber material that uses crumbs from discarded tires. GreenMan uses it to produce water filters, pumps, stereo components, and computer accessories.

On Dec. 14, Browning-Ferris Industries, a major player in solid-waste collection and recycling, signed an exclusive contract for GreenMan to build and operate a crumb-rubber processing facility on Browning's site in Jackson, Ga. It will convert a minimum of 32,000 tons a year of shredded tires into high quality crumb rubber. Browning-Ferris may buy an equity stake in GreenMan, speculates one analyst.

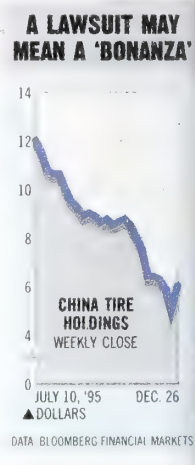
Revenues for the year ending May 31, 1996, are expected to be $7 million to $10 million, in part from a $2 million contract with Coca-Cola—for GreenMan to make display racks of recycle rubber. One analyst sees GreenMa going into the black in 1996.

CHINA TIRE MAY BE UNDULY DEFLATED

On the Big Board, China Tire Hol ings (TIR) behaves as if it were retread. In early summer, shares this major Chinese tiremaker wer around 12. They're now at 6, and eve Morgan Stanley downgraded its ra ing in November to "neutral" from a earlier "buy." That's quite a blow: Mo gan Stanley was one of China Tire major underwriters when it went pu lic—in July, 1993, at 17 a share. And owns 5.7% of the stock. Constantl shifting U.S.-China relations are pa of the Street's aversion to the stoc And there has been concern about Ch na Tire's earnings predictability.

But not everyone is down on th stock. Investment manager Bill Ha nisch has been buying since the stoc hit 8 in September—and bought eve more when it dropped to 6. How come

"For a company with an estimate book value of more than $15 a share the stock is very cheap," says Ha nisch, president of Forstmann-Leff, a New York investment firm managing about $3 billion. And in spite of the poor performance of most other Chinese tire biggies—caused in part by a drop in car sales—China Tire's revenues in most of 1995 jumped by more than 33%, and its earnings grew by 10%, he notes. Harnisch estimates 1995 earnings a 50¢ a share. For 1996, he foresees earnings of 75¢.



And then, there is the "bonanza tha we expect China Tire could win fro its lawsuit filed against Goodyear i the U.S.," says Harnisch. China Tir claims that Goodyear interfered wit its contract to buy a radial-tire factory in China owned by Dalian Genera Rubber Factory: Goodyear bought the factory instead. Some analysts believe Goodyear Tire & Rubber faces a $3 billion penalty if it loses the legal fight

Was it a *midlife crisis?*

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The Top MANA

What did it take for an executive to succee in the past year?

Good managers know how to cut: They trim costs, reengineer, and restructure. Great managers know how to grow: They realize you can't shrink your way to greatness. In 1995, the best managers in the world grew their way to greatness.

The men and women of BUSINESS WEEK's Top 25 Managers of the Year—Americans, Europeans, Asians—all rode the tiger of growth to spectacular success. In a global economy of vast technological change, intense competition, and political upheaval, these managers cranked out annual increases of 20%, 30%, sometimes even 40% in profits and sales—while other corporate "titans" were still trimming their sails and eking out marginal gains.

What did it take for an executive to make it into BUSINESS WEEK's Top 25? Begin with product innovation—the hot strategy of the year for managers who had already wrung out their corporate inefficiencies. When the bureaucratic layers are gone, when the marginal competencies are dumped, the only strategic assets left to corporations are the products they sell in the global marketplace. This was proved in 1995, when the most reliable path to fast growth was to bring out new products adored by lots of consumers.

Riding the technological currents was the favorite tactic used by managers in bringing out their innovations in 1995. But managers also had to take risks, especially the risk of cannibalizing old models with new products. There was new software for personal computers and the Internet, color copier/printers for the home office, and even new first-class seats that fold out into beds. All were smash hits.

BUSINESS WEEK's top managers used corporate alliances to drive their growth. American and European managers divvied up the incredibly successful DBS launch—direct broadcast satellite transmission of TV and stereo music. A French-owned company built the 12-inch satellite dishes for the home, and the Americans developed the satellites and software to close the loop.

The Best MANAGERS/52 MANAGERS TO WATCH/58 EN

Nearly two million homes in the U.S. now have DBS. This global cooperation generated tremendous growth for all concerned. So did alliances between industries: One software giant linked up with a corporation running a TV network to provide new information products over the wire.

Top managers used globalization strategies wisely to boost growth. Asian territories outside Japan proved once again to be the fastest-growing markets in the world in 1995. Every smart manager wanted a bigger piece of the Asian pie. Some succeeded, as did one investment banker who was able to cut a deal enabling his firm to

ROBERT AYLING British Airways
MIKE ARMSTRONG Hughes Electronics
ANA BOTIN Banco Santander
CASEY COWELL US Robotics
GEORGE DAVID United Technologies
MICHAEL EISNER Walt Disney
GEORGE FISHER Kodak
WILLIAM AND VICTOR FUNG Li & Fung
ANDREW GROVE Intel
GERALD GREENWALD United Airlines
RALPH LARSEN Johnson & Johnson
JAN LESCHLY SmithKline Beecham
JOHN MACK Morgan Stanley
ARTHUR MARTINEZ Sears Roebuck
SCOTT McNEALY Sun Microsystems
PAUL O'NEILL Alcoa
BERND PICHETSRIEDER BMW
LEW PLATT AND RICHARD BELLUZZO HP
ALAIN PRESTAT Thomson Multimedia
JEAN-PIERRE ROSSO Case
TADASHI SEKIZAWA Fujitsu
STAN SHIH Acer
WILLIAM SIART First Interstate Bank
WILLIAM STEERE Pfizer
PATTI STONESIFER Microsoft

business inside China. Another American manager reversed strategy and revitalized his heavy capital equipment company by focusing on new opportunities in Europe.

Then there were Asian managers using the global markets to move outside their region into other parts of the world. One computer maker divided his operation into 21 smaller companies so that each could list on the stock market where it did most of its business.

Of course, reengineering remained important as a catalyst for growth for some top managers. One new Japanese manager quietly restructured ingrown business practices of his company and led it to a projected doubling of net profit and a record year. An American continued to reshape a traditional defense-base conglomerate into a tough market-oriented competitor.

How did BUSINESS WEEK come up with its Top 25 Managers of the Year? The magazine polled its 220 editors around the world, including its large foreign bureau system, the largest of any global business magazine. The methodology was deceptively simple: screening the financial figures, questioning the best analytical minds, and talking to the leading corporate managers around the world. The bureaus asked: Who was the best in 1995? Here's the collective reply.

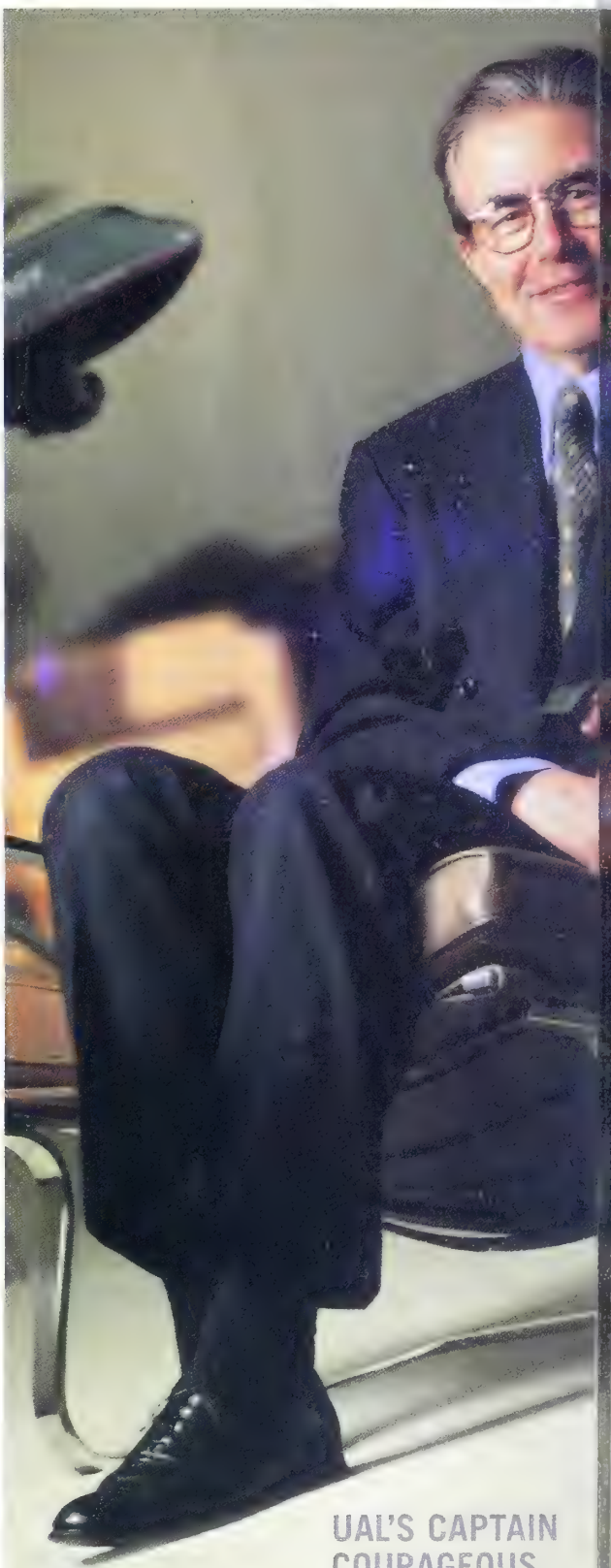
NEURS/62 NEW PRODUCTS/64 PRODUCTS TO WATCH/71

The Best MANAGERS

Managing big corporations in 1995 was tougher than ever. It was hard to raise prices, technological change accelerated, and globalization meant more competition. Achieving growth meant taking more risks. These 25 managers were the top winners in the global game.

BEAUTIFUL BEEMER

▲ **BERND PISCHETSRIEDER,** BMW's new CEO, surprised everyone by getting BMW's new American-made Z3 roadster featured in the latest James Bond movie, *GoldenEye*. In 1995, Pischetsrieder, 48, drove BMW into the big leagues as a million-unit-a-year producer with a new auto plant in the U.S. Sales in the U.S. zoomed to over 90,000 Beemers, the best since 1986's record.



UAL'S CAPTAIN COURAGEOUS

▲ It isn't easy running employee-owned airline **GERALD GREENWALD,** c man of UAL, managed t lots of people happy in

e than doubling the
rice, to $211, Green-
), put big smiles on
stors: Wall Street,
nd machinists, al-
fourth-quarter earn-
imates didn't meet
s' expectations.
gs are still expected
bout $900 million,
994's figure.

MICROSOFT'S OTHER DYNAMO

◀ **PATRICIA Q. STONESIFER** put Microsoft's Consumer Div. on the map in 1995. The 39-year-old manager, known for "crisp" thinking, drove the division to launch 20 new CD-ROMs and software products for the home, including Fury3—Microsoft's first shoot-'em-up game—and a souped-up joystick called Side Winder. The division had estimated sales of $800 million, making it the country's No. 1 multimedia company.

ACER'S ACE IN THE HOLE

▲ With the booming sales of Acer's Aspire personal computer, a multimedia desktop designed for the home, Acer Chairman and CEO **STAN SHIH** solidified his position in 1995 as Asia's paramount entrepreneur. By decentralizing ownership (he is spinning off 21 independent companies), Shih remains close to his customers. Revenues for the Taiwan-based group in 1995 are expected to be up 77%, to $5.7 billion.

SUPERCALIFRAGILISTICEXPIALIDOCIOUS

◀ **MICHAEL D. EISNER,** chairman of Walt Disney, showed in 1995 he could do it his way, without close pal and President Frank G. Wells, who died in a helicopter crash in 1994, or studio chief Jeffrey Katzenberg, who left in anger. The 53-year-old Eisner made a $19 billion deal for Capital Cities/ABC, lifting Disney to global media's top tier. Theme parks are minting cash anew. Even EuroDisney turned a profit.

The Best MANAGERS

RECHARGING THE BIG STORE

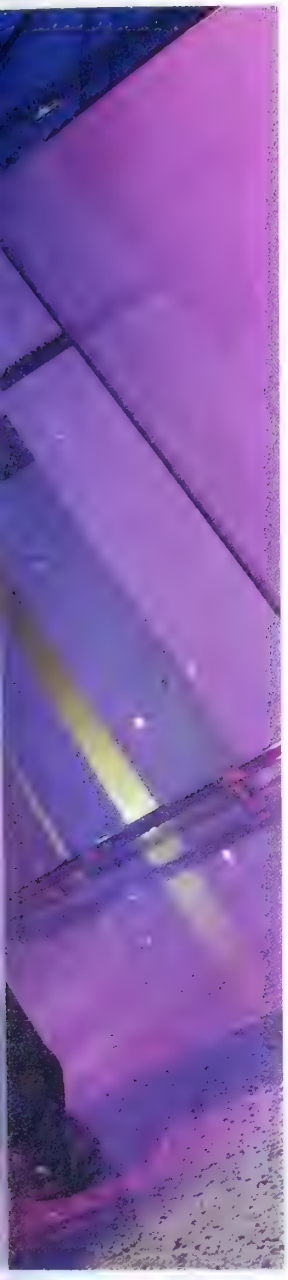
▶ It all came together in 1995 for **ARTHUR C. MARTINEZ,** CEO of Sears Roebuck and the mastermind of the Big Store's comeback. His drive to renovate dowdy outlets and upgrade women's apparel paid off with big revenue hikes last year as rivals floundered. His risk-taking was duly rewarded. Martinez, 56, was named chairman of the parent in July.

GATES-CRASHER

▼ Hot Java! Sun Microsystems CEO **SCOTT G. McNEALY** went eye to eye with Bill Gates in 1995 with Java, the revolutionary Internet software. But that was just icing for McNealy, 41. Sun's "servers" became serious contenders in corporate computing. For Sun, it meant an 82% rise in profits, to $356 million, on sales of $5.9 billion in fiscal 1995.

GOOD SHOW, BLOKE

▶ **ROBERT AYLING,** British Airways' managing director, ran one of the world's most profitable airlines in 1995. His reward: being made CEO as of Jan. 1. BA is expected to report $890 million in pretax profits on sales of $12 billion for the year ending March, 1996. Smashing! Ayling, 49, skipped college and climbed the corporate ladder without family or school ties. He now must decide whether to put more money into USAir.



LIKE FATHER, LIKE DAUGHTER

▲ **ANA PATRICIA BOTIN,** 35, is chief executive of Spain's Santander Investment. Botín shares the penetrating gaze and workaholic drive of her father, Emilio, chairman of Banco Santander. In using Santander's strong capital base in Latin America, Botín has built market share and won for Santander the lead role in bringing Mexico back to the capital markets.

TEMPUS FUJITSU

◀ For **TADASHI SEKIZAWA,** 1995 was the year Fujitsu finally cast off the shackles of a weak economy and soaring yen. Sekizawa, 64, restructured ingrown business practices and dumped nationalistic policies. Fujitsu starting selling PCs built 90% with non-Japanese components. It expects to double group net profit to a record $887 million.

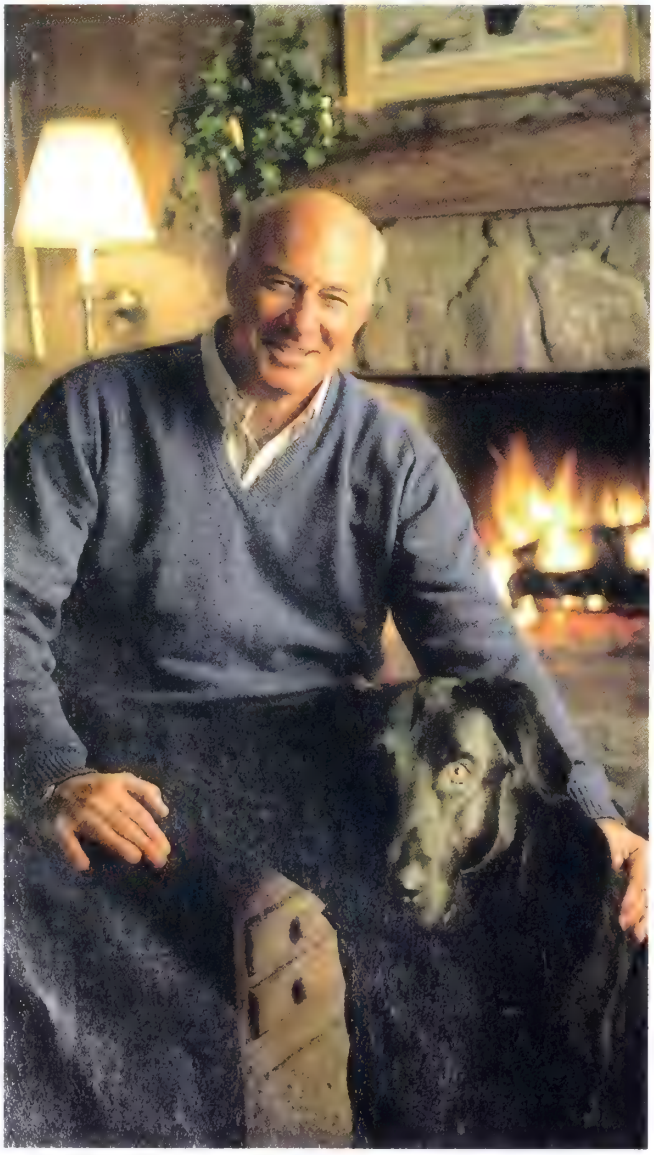
The Best MANAGERS

WHY SMITHKLINE FEELS SO GOOD

▶ **JAN LESCHLY,** CEO of Anglo-American drugmaker SmithKline Beecham, spent 1995 digesting $5 billion in acquisitions of managed-care and consumer-medicine markets, then turned his attention to heartburn—by managing the transition of ulcer drug Tagamet, once the world's largest-selling drug, to over-the-counter. SKB's sales could hit $10 billion in '95.

BEATING SWORDS INTO SITCOMS

▼ **C. MICHAEL ARMSTRONG,** CEO of GM Hughes Electronics, has led a great new product launch—DirecTV, a satellite-to-home television service that beams crystal-clear programming to rooftop dishes. Armstrong took a stodgy military contractor and used its high-tech smarts to tap into new commercial markets. The stock is up 50% on the year.



EAST MEETS WEST AT LI & FUNG

▶ **WILLIAM AND VICTOR FUNG,** top-notch managers of Li & Fung, are members of a new Asian corporate elite. William, 46, is a Princeton grad with a Harvard MBA, while Victor, 50, is a Massachusetts Institute of Technology grad with a Harvard PhD. The brothers are converting their Chinese-style family export-trading business, into a modern, publicly owned corporation. In 1995, they bought British rival Inchcape Buying Services, doubling Li & Fung's annual sales, to $1.5 billion.

LIFTING CASE'S HEAVY LOAD

◀ When **JEAN-PIERRE ROSSO** took over heavy-equipment manufacturer Case in 1994, it hadn't turned much of a profit in years. Cost-cutting by parent Tenneco stopped the bleeding, but there was no strategy. He redesigned Case's outdated construction- and agricultural-equipment lines and focused on Europe. The payoff? Earnings in 1995 should double, to $250 million, on an 11% hike in sales, to $4.8 billion.

SHINING UP ALCOA

▲ In early 1994, an avalanche of cheap Russian metal threatened to bury America's world-leading aluminum companies. Aluminum Co. of America's CEO, 60-year-old **PAUL H. O'NEILL,** pushed for a multinational solution, which included painful smelter shutdowns in the U.S. He also pressed forward with global acquisitions, from Italy to Australia. With aluminum prices on the rebound in 1995 and world supply and demand on a more even keel, Alcoa motored to strong earnings.

The Best MANAGERS

YOU CAN BANK ON THIS CEO

▶ **WILLIAM E.B. SIART** of First Interstate Bancorp is such a good manager he's about to lose his job. As bank president since 1990 and CEO since January, Siart, 48, helped turn the lender around, raising shareholder return on equity from a dismal –10% in 1991 to 26% last quarter. Now, Wells Fargo and First Bank System are vying for Siart's bank.

THOMSON'S FAVORITE DISH

▼ **ALAIN PRESTAT,** CEO of Paris-based Thomson Multimedia, provided the amazing $599 12-inch dish and set-top box that made direct satellite broadcast one of the biggest hits of 1995. Thomson's RCA Digital Satellite System sold nearly 2 million units in a year. Operating profits jumped fourfold. Next up: new Digital Video Disks with more capacity.

Managers to watch in 1996

JOHNSON

■ Abigail Johnson, 34, is heir very apparent at Fidelity Investments. The boss's daughter owns 24.5% of Fidelity. That makes her a billionaire, but is she a manager capable of taking over from Dad, Edward C. "Ned" Johnson III, who is 65? So far, Abby has dodged a role in senior management to manage money. Will she become chairwoman and leave day-to-day management to others? ■ Eric A. Benhamou, chief executive officer of 3Com, loves to manage—other businesses, that is.

BENHAMOU

He is Silicon Valley's gentlest takeover artist. His 3Com pulled off 10 acquisitions worth $1 billion in three years. Now he's trying to persuade Wall Street that he can make money in the expanding market for lower-end networking gear and PC network cards for small busine the home. Tired of slowpoke modems? Call hamou. ■ Ford Chairman Alex Trotman pr has the toughest job in Detroit in 1996. Cu ers aren't stampeding to his newly styled T Ford is overhauling 40% of its entire U.S.

TROTMA

A GIANT'S MOST GIANT STEP YET

▲ **ANDREW S. GROVE** made 1995 the year Intel moved beyond merely being the world's biggest chipmaker to being the biggest force in the entire computer industry. Grove, 59, pushed into motherboards, logic chipsets, and even entire computers. Intel's next targets include engineering workstations and large servers. Its 1995 sales are expected to be up more than 40%, to $15 billion.

PLENTY OF FIZZ IN PFIZER

◀ For **WILLIAM C. STEERE JR.**, 59-year-old CEO of Pfizer, the big payoff came in 1995. He sold off nondrug operations and refused to shell out billions for distributors, as rivals have. Instead, the avid helicopter skier has focused on riskier new products. Driven by antidepressant Zoloft and antihypertensive Norvasc, Pfizer's net income in 1995 rose 20%, to nearly $1.56 billion, while sales gained 23%, to $10.2 billion.

and 35% of its European offerings. Trot- under pressure to find a way to move all ew, more expensive models in a market nterested only in bargains. Will lower ve Trotman some breathing room by cutsing costs? ■ In April, 1995, Nobuyuki

Idei, 58, became the first nonengineer to lead Sony, replacing Norio Ohga. He quickly dumped Mickey Shulhoff, Sony's high-profile U.S. head. Idei speaks fluent English and French, but it has yet to be seen whether he can speak Hollywoodese. ■ Bill Gates faces his biggest challenge in years. While the 40-

GATES

year-old chairman of Microsoft has the PC software market sewn up—not so the mushrooming Internet world. In December, Gates mapped out an ambitious Internet strategy. Then he licensed Java, the hot Internet software. Is this a new beginning or the end of his hegemony? ■ For as long as Jerry Levin has been chairman of Time Warner, investors have wondered if he had the "it" of leadership. This fall he acted boldly and acquired Turner Broadcasting System. But now he has to stir up that magic synergy, something he couldn't do between Time Inc. and Warner. Is this his last shot?

LEVIN

The Best MANAGERS

KODAK CLICKS AGAIN

▶ **GEORGE M.C. FISHER** started to prove in 1995 that Eastman Kodak's core photography business still had vigor by boosting consumer-imaging revenues 19% for the first nine months. Also, he filed a complaint that Fuji Photo conspired with Japan's government to limit Kodak's share there. Kodak stock, up 39%, is back as a Dow leader.

CAPITAL IDEAS FOR MORGAN

▼ In one of Wall Street's best years ever, Morgan Stanley Group President **JOHN J. MACK** had a nice one of his own. Mack, 51, forcefully integrated independent departments. It worked. The firm's stock rose 43%, and its earnings soared 73%. Under Mack, Morgan became the only foreign investment bank allowed to do business inside China.

Managers to watch in 1996

SCHULMEYER

■ Gerhardt Schulmeyer, chief executive at German computer and telecom company Siemens Nixdorf Informations Systems, is aiming to topple Big Blue in Europe. But can he break the great resistance to change within Germany's telecom industry? If Schulmeyer can't do it in 1996, Germany will only fall further behind. ■ Whoever thought an obscure animal-feed ingredient could lead to so much fuss? But for Dwayne O. Andreas, chairman of Archer Daniels Midland, lysine could be his Waterloo. Federal antitrust investigators are reviewing hours of taped conversations provided by a former employee, Mark Whitacre, who claims ADM fixed lysine prices.

ANDREAS

Meantime, under fire from shareholders, Andreas, 77, has appointed a committee of outside directors to put A corporate governance under a microscope. C survive another year? ■ Ditto for Michael H Spindler. With first-quarter results ending D in the red, following a year of takeover rum and boardroom turmoil, Apple Computer's e

SPINDLE

J&J GOES ON THE OFFENSIVE

◀ Johnson & Johnson Chief **RALPH S. LARSEN** doesn't shrink from a fight. In 1995, he won J&J's first-ever hostile takeover battle, snaring Cordis. Using ads that slammed a rival's product, Larsen also turned an obscure Merck prescription drug, Pepcid AC, into an over-the-counter heartburn powerhouse. J&J had one of its most profitable years on the 57-year-old CEO's watch. Net income is expected to be up 19%.

HELPING UTC TO CATCH THE WIND

▲ For **GEORGE A. DAVID,** an ocean sailboat racer, 1995 was the year his company finally delivered. United Technologies saw earnings and margins rise despite falling defense spending and modest revenue growth. The 53-year-old CEO galvanized the $21 billion conglomerate to capitalize on its great name franchises—Otis, Carrier, Sikorsky, and Pratt & Whitney. Wall Street cheered: The stock rose about 48%.

is hanging on by a thread. The board is him for now. ■ Insiders says W. James ey Jr., a 46-year-old Yale graduate and MBA, is a front-runner in the race to suck Welch as CEO of General Electric. In Oc- elch pulled McNerney away from a critical post as head of GE's Asia operations to take over management of the $3 billion lighting unit. ■ Lester M. Alberthal Jr. may soon find himself running an independent Electronic Data Systems, the information services giant in Plano, Tex. EDS has been part of General Motors since 1984, when it was sold by famous founder Ross Perot. GM announced in August, 1995, that it planned to spin off EDS if it can get the Internal Revenue Service's approval for a tax-free deal. Analysts expect EDS's independence day to come by the spring. ■ When you're running for your life, do you reach for a Snapple or a Gatorade? William D. Smithburg, CEO of the Quaker Oats, has his hands full with both. His dominant Gatorade franchise faces a terrific challenge in '96 as Coca-Cola promotes its rival sports drink, Powerade, at the 1996 Olympics. He has even knottier problems with his Snapple franchise.

ALBERTHAL

:Y

SMITHBURG

MODEMS FOR THE MASSES

▶ He's chairman of the hottest U.S. modem manufacturer. Thanks to the explosion of computer networks, **CASEY G. COWELL's** U. S. Robotics saw revenues explode to $889 million in 1995, up from $378.6 million in '94. Cowell, 43, built new plants and designed faster modems. He also bid for bankrupt Hayes Microcomputer Products, once the country's largest modem maker. Cowell is shooting for a $5 billion company by 2000.

ONE-TWO PUNCH AT H-P

▲ How do you make a huge company grow 20% a year? In 1995, Hewlett Packard CEO **LEWIS E. PLATT** showed 'em how again. Sales are up 26%, to $31.5 billion; profits are up 52%, to $2.4 billion. Platt, 54, tapped **RICHARD E. BELLUZZO,** 42, to merge the retail-minded PC and printer division with the old Big Iron business. Platt believes corporations want one-stop shopping for information technology, and he's giving it to them.

Managers to watch in 1996

OKUDA

■ Can Hiroshi Okuda cure Toyota's big-company disease? In August, the 63-year-old finance man became president of Japan's largest auto maker, the first non-Toyoda family member to run the company. Many see the bold executive as the best hope for a fresh breeze at Toyota. ■ Can a power-tool marketing whiz finally put some drive back into Polaroid? On Dec. 1, 44-year-old Gary T. DiCamillo took the reins as the new CEO. Given credit for reviving Black & Decker's consumer power tool business, he's now charged with resurrecting a company that has been drifting sideways for years. ■ Journalists recoiled in 1995 as new Times Mirror CEO Mark H. Willes closed *New York Newsday* and ordered layoffs at the flagship *Los Angeles Times*. Willes, a 15-year veteran of General Mills, was brought in to repair years of sluggish profits at Times Mirror. His goal: boost earnings per share by 50% in 1996.

DiCAMILLO

WILLES

Connect

"The advantage we give our clients in emerging economies isn't just that we know the markets. It's also that the markets know us."

J.P. Morgan bankers in Bombay with joint venture colleague (center)

When you're doing business in emerging markets, it helps to be known – by potential partners, government officials, and others who can make or break a deal. Our long-time involvement in virtually every sector of these markets ideally positions us to share insights and deliver successful outcomes. Consider these recent credentials: we were sole lead manager for Poland's first international debt issue since 1989. In South America, we advised on the largest M&A transaction (outside of privatizations) of 1995. We helped the world's largest auto maker enter the market in India, where joint ventures of our own give us a unique presence. As a trader of securities from more than 40 emerging economies, our 1994 volume was double that of our nearest competitor. The fact is, no other firm is as active across the board. So J.P. Morgan clients get more than an outpost in the emerging markets. They get a sponsor who can help them connect with the right information, the right opportunities, and the right results.

Our widely followed *Emerging Markets Bond Index Plus* is now available on the World Wide Web at http://www.jpmorgan.com

JPMorgan

The Best ENTREPRENEURS

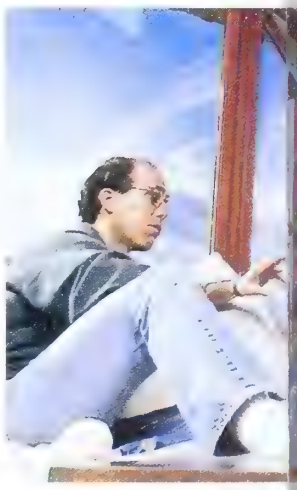
An amazing year for entrepreneurs! A new club was formed: double-billionaire winners. Jim Clark did it once with Silicon Graphics and came back with Netscape. Steve Jobs hit it big with Apple–took a long break–and won again with Pixar. The hurdle was certainly raised in '95.

SECURE SOFTWARE FOR THE NET

▲ **SHIKHAR GHOSH,** Open Market's 38-year-old chairman and co-founder, allows dogs in his company's Cambridge (Mass.) offices, but that's his only quirk. Open Market builds secure software for critical commercial applications on the Internet. It has helped set up the hottest commercial Web sites, including those of Banc One and Ziff-Davis, which rely on Open Market's software for handling credit-card transactions and filling orders. Ghosh may be the one holding the keys to really doing business on the Net.

JOY STORY

▲ How sweet it is. **STEVE JOBS,** co-founder of Apple Computer, has been trying to come up with a second hit for a decade. No such luck—until Nov. 29. That's when his company, Pixar Animation Studios, makers of the smash hit movie *Toy Story*, went public with a bang. The stock, priced at 22, zoomed to 49 before falling back to 24. Jobs's 80% stake was briefly worth $1.1 billion. What's next? His other company, NeXT, is making Web software, and Jobs may see his third IPO in early 1996.



THREE MEN AND A $2 BILLION BABY

▲ Not many companies start life with $2 billion in capital. But then, not many upstarts come wit **JEFFREY KATZENBERG, STEVEN SPIELBERG,** and

D GEFFEN. Hollywood's mWorks company will 1 1996 with a new com- ɔn ABC and a George ael album. Down the *Prince of Egypt*, an ated film about Moses, nteractive games with ɔsoft.

C'EST MAGNIFIQUE

◀ **DENIS PAYRE** and **BERNARD LIAUTAUD,** both 33, are two French entrepreneurs every American venture capitalist would be glad to have discovered. Their Paris-based software company, Business Objects, is No. 1 in the fast-growing decision-tools market. It "IPO'd" at 17½ in 1994 and hit a 52-week high of 54 in 1995. Sales and profits boomed with the launch of a sizzling second generation of products.

THE GREAT 'SCAPE

▶ **JAMES H. CLARK,** 50, founder of Silicon Graphics, has done it again. His Netscape Communications makes the Internet's top software. Clark took it public 18 months after founding it with cyberwizard **MARC L. ANDREESSEN,** 24. Its market cap is now $5 billion. Now, that's an IPO!

PRIDDY IMPRESSIVE

◀ The third time's a charm for **ROBERT PRIDDY,** who founded two other airlines before creating ValuJet Airlines. Using unorthodox techniques like ticketless travel, flying secondhand DC-9 aircraft, and maintaining a low-frequency route system, Priddy has helped ValuJet grow to $350 million in sales, with regular service to 26 cities. Earnings should hit $57 million in 1995.

The Best NEW PRODUCTS

Product innovation was the key to growth in 1995. And boy, were there great products! Hot Web sites and CD-ROMs captured imaginations, but there was also room for jazzy cars, toys for grownups, and the laptops, pagers, and other stuff needed for work these days.

A BIKE FOR ALL MOUNTAINS

▲ Electric Bicycle's E Warrior is a battery-powered electric mountain bike that hums along at 20 mph and has a range of 15 miles. Price: $800 to $1,400.

AN EXEC MARCHES ON HIS SEAT

◀ Herman Miller's award-winning Aeron chair features space-age materials and adjustable height, armrests, hip pivot, and lumbar support. The eye-catching piece costs $700.

FITS IN A TIGHT SPOT

◀ Packard Bell Electronics' Corner Computer offers wing-style disk drives that eliminate the problem of CD-ROM trays that spill out over the top of the keyboard. The price starts at $1,899.

FOR THE TROUT IN YOUR LIFE

▼ To a fly fisherman, the Sage RPL+ rod is the last word in yin and yang. The rod is strong yet sensitive to the slightest nibble. Line running through the rod can handle weight and still form a graceful arc. Cost: $400 to $500.

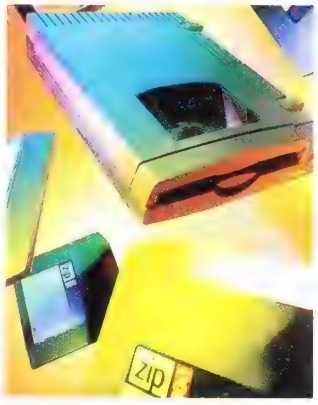
ONE FOR THE MONEY

Intuit's newest Quicken software lets users bank online from home, pick mutual funds, and otherwise tackle personal finance chores. The new $60 Quicken Deluxe CD-ROM also includes Finance 101 section to help demystify money management.

Quicken DELUXE
Organizes Finances Painlessly

FLOPPIES MAY BE ENDANGERED

▶ Few tasks are more time-consuming than copying data from your PC's hard drive onto floppy disks. But Iomega's $200 Zip add-on drive stores 100 megabytes—70 times as much as a floppy—on one $20 removable disk.



HARD WORK, BIG FUN

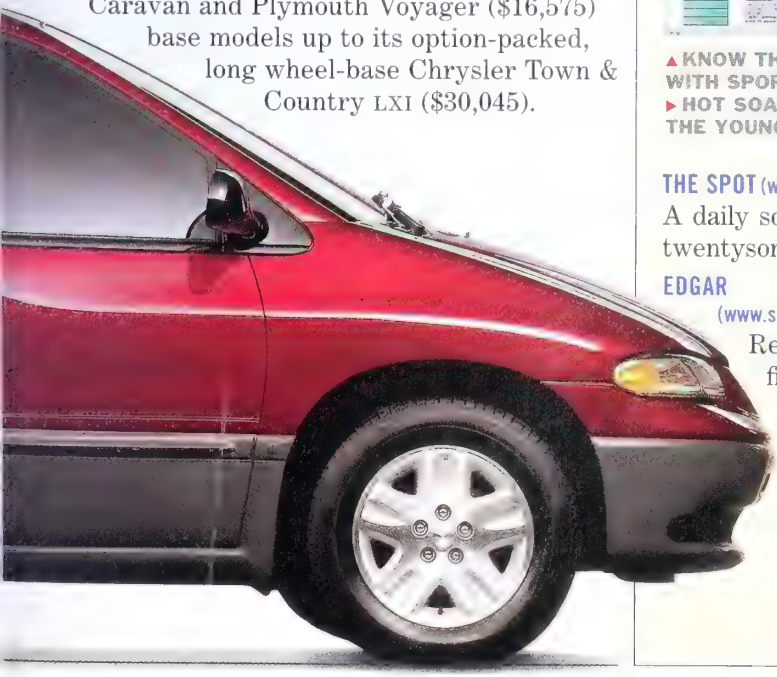
▲ Sony's hot new game machine, Play Station, expands the meaning of "play." Mastering the sophisticated controller and CD-based action games is hard work, but the 3-D graphics are stunning. Price: $299 for the console.

OLTIN' JAVA

It's the hottest Internet software on the planet. Java, a new programming scheme from Sun Microsystems, is shaking everyone up—including Microsoft.

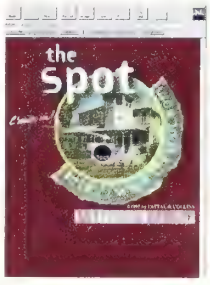
A GIANT LEAP FOR MINIVANS

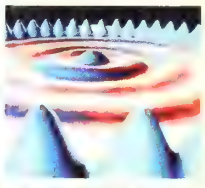
Chrysler invented the minivan segment, but it has broken the mold with its completely redesigned new model. Hottest new feature: the driver-side sliding door, an option rivals are scrambling to copy. Handling and suspension are dramatically improved. Chrysler covers all the price points, from its Dodge Caravan and Plymouth Voyager ($16,575) base models up to its option-packed, long wheel-base Chrysler Town & Country LXI ($30,045).



the best/web sites

▲ KNOW THE SCORE WITH SPORTSZONE
▶ HOT SOAP FOR THE YOUNG SET





▲ BREATHTAKING PORTRAITS OF ATOM BEAUTY

THE SPOT (www.thespot.com)
A daily soap opera about twentysomethings.

EDGAR (www.sec.gov/edgarhp.htm)
Repository for SEC filings by companies since '94.

CENSUS (www.census.gov)
If it's demographic information you want, this is the place.

ESPN SPORTSZONE (espnet.sportszone.com)
Up-to-date scores of college and pro games.

WOODROW (woodrow.mpls.frb.fed.us)
Federal Reserve Bank of Minneapolis' site has tons of financial info.

IBM's Almaden Reseach Center (www.almaden.ibm.com:80/vis/stm/gallery.html)
Breathtaking portraits of atoms, made by scanning tunneling microscopes.

IN THE FIERY CAULDRONS *of the Ohio Valley, a newly competitive company has been built.*

By reworking business practices and rethinking computer systems, AK Steel now yields more profit per ton of steel than any other steel company in the United States.

Consultants from IBM's wholly owned subsidiary ISSC w in partnership with AK ma in operations, finance and

The result? An improv information system, manag

Create

and a single-minded focus
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BM-3333, ext. H 1025. Or stop
by our home page at http://www.issc.
ibm.com

Solutions for a small planet

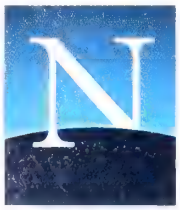
The Best NEW PRODUCTS

THE EYE HAS IT

▲ Canon's ES5000 Eye Control camcorder does just that—it lets you eye-activate focus shifting, quick zoom, and other features. Whatever you look at stays in focus. This top-of-the-line model, with Hi-Band, 8mm resolution is priced at $2,200.

NET GAINS

▼ It changed everything on the Net. The power of Netscape Communications' Navigator software is remaking the entire information industry. Thanks to fast downloading and enhanced graphics, it's widely considered the best "browser" for surfing the World Wide Web. Available for free on the Net, Navigator



now commands 70% of the Web browser market—far surpassing its predecessor, Mosaic, which was invented by Netscape cofounder Marc L. Andreessen. It's a tenuous lead, because nearly everyone, including Microsoft, is aiming at Netscape.

SO WHO NEEDS A PHONE?

▲ Motorola's Tango Two-Way Paging System is the first pager of its kind: It allows businesses and individuals to respond to their pagers without having to get to a phone. Users can simply select from a menu of up to 120 preprogrammed messages. Through Skytel, the service provider for Tango, the price for national service starts at $74.95 per month. Cost of the pager alone: $399, or $15 a month to lease.

A MULTIMEDIA MAC FOR ALL SEASONS

▼ Apple Computer's Macintosh Performa 5215CD is an all-in-one multimedia PC. Its 15-inch screen can be tilted and swiveled. It fits nicely in the home, with a single cable containing power cord and printer hookup that lets it scrunch right up against walls, saving desk space. The 5215 has a remote control for CD playing or TV viewing. Price: $2,000.

THE LONG, LONG RACKET

▲ The 1970s gave tenn buffs the oversize racket; 1980s, the widebody; and nov the 1990s, there's the extralong. With its Max series, Dunlop Slazer ger led the pack with the newest rack technology, adding 1½ inches to the standard 27-inch frame. It's 125 square inches—15 more than most bi rackets. At 9½ ounces, the extralongs are extremely light. They're best suited to average-size men, senio beginners, and women who don't pound the ball and want a little more on their serve. Price: $225.

HANDS UP, YOU LOUSE!

◀ Putting in a long night? Break the stress with the air-owered Burp Gun, a ecreation of the 1950s ng-pong ball shooter at boomers remember. reat *braaap!* sound hen you squeeze off a und. Price: $19.95.

COLOR COPIES FOR A SONG

◀ It hit shelves in December, and already Hewlett-Packard's CopyJet is making waves. Home-office and corporate types are grabbing the gizmo, both a color printer and copier, rather than schlepp to Kinko's for color. At $2,500, it beats the $20,000-plus machines on the market. HP figures color copies run 7¢ on this baby, vs. $1 to $1.50 at an outside copy center.

MOVE OVER, MR. ANDRETTI

▼ Blasting off in the new Porsche 911 Turbo is the closest you'll probably get to driving a real race car. A pulse-revving 400 horsepower in the '96 model gets it from 0 to 60 miles per hour in 4.4 seconds. Top speed is 180 mph. Price: a cool $105,000.

the best/cd-roms

WITH *3-D MOVIE MAKER*, KIDS CAN BECOME *AUTEURS*

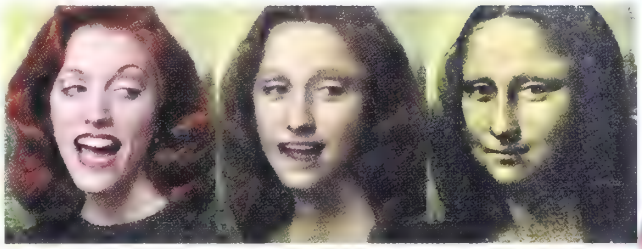
So your son wants to be the next Spielberg? Microsoft's Windows 95 CD-ROM *3-D Movie Maker* ($44.95) lets kids create 3-D films on PC. ■ Art lovers like to see works from many perspectives. Corbis Publishing's *A Passion for Art* is a splendid $40-to-$50 CD-ROM that takes them through the Barnes collection. ■ Delrina's *Echo Lake* is a cozy $60 program for housing photos, videos, and sound clips of your loved ones.

ONE PRETTY PICTURE

▲ The titanium-clad Contax G1 is a classic range finder camera with state-of-the-art automation. It has a beautiful retro look and accepts four interchangeable Carl Zeiss lenses. Price for the body: $1,500.

FLEXIBLE FLYER

▶ After three years of development and a battle with Bombardier, the Gulfstream V is corporate globetrotters' hot new tool. The G-V, which seats 12 to 19 and retails for $35 million, can fly nonstop from New York to Tokyo, 6,500 nautical miles.



SNAPPY SHOTS

▲ Want a photo of dear-Aunt Martha on your PC? Play Inc.'s $200 Snappy plugs into a PC and links to a camcorder, VCR, or TV. Click to freeze a frame that can be enhanced or morphed on the PC.

NOTEBOOK NONPAREIL

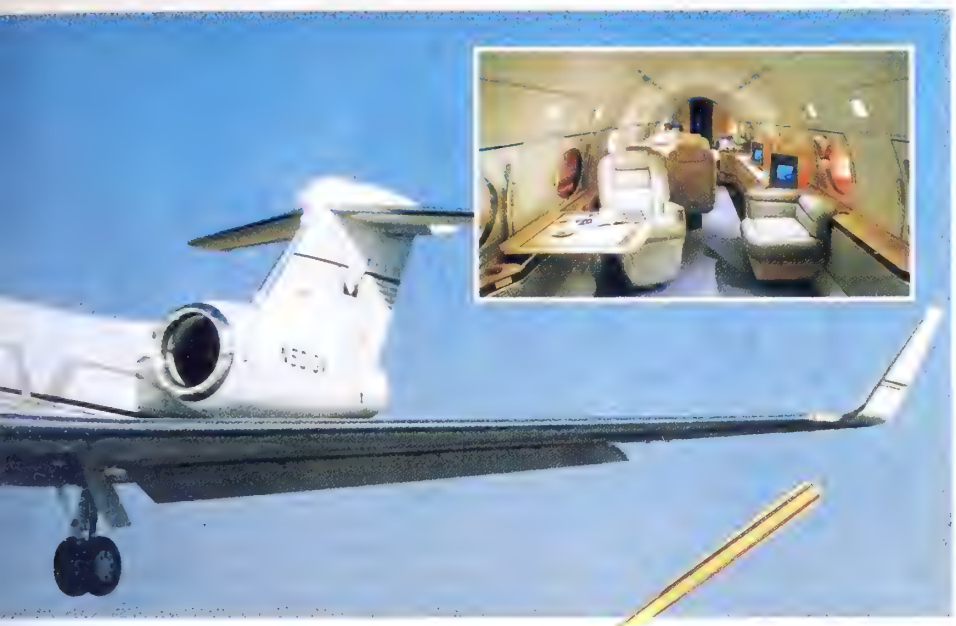
▲ IBM's ThinkPad 760CD is the ultimate notebook computer. The brilliant 12.1-inch color display and advanced video features allow Hollywood and ad agency types to view commercials or the daily rushes. Price: a hefty $7,500.

DOUBLE-DUTY DRIVER

▲ The Taylor Made Burner Bubble is one of the hottest drivers on the golf course. Taylor Made Golf shifted weight on the shaft from under the grip a couple of inches toward the head. That hikes centrifugal force and clubhead speed during the swing. A low center of gravity moves the ball into the air fast and allows the driver to double as a jazzy fairway wood. Price: $299 for steel, $499 for titanium.

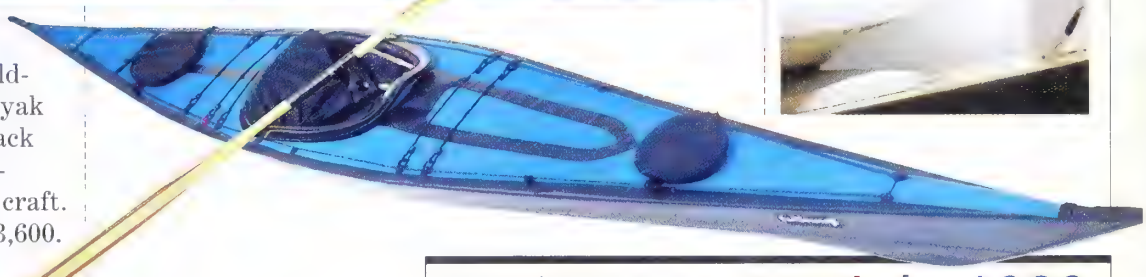
BOOMING BOX

▼ A no-show in home PCs until 1995, Hewlett-Packard is on track to hit the top three by '97, thanks to the Pavilion. It allows each family member to set up his or her own library of commonly used software. Price: $2,100 to $3,500.



O TOY BOAT

Feathercraft's fold- Khatsalano-S kayak n fit into a backpack d open into a full- ngth, sea-touring craft. Price: $3,600.



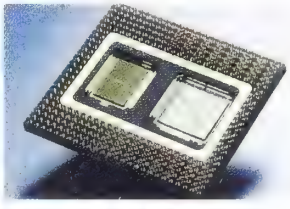
RELIVING YESTERDAY'S TRIUMPHS

The Triumph Thunderbird 900 is a redo of the legendary Triumphs of the '50s—presumably without the equally venerable oil leakage and electrical problems. The guts are all modern, with three- and four-cylinder multivalve engines. The 885 cc Speed Triple will bring joy to any leather-clad office-bee craving thrills. Price: $9,995.

products to watch in 1996

Cadillac is counting on its new German-engineered, entry-level Catera sedan to entice boomers away from the Lexus and the Beemer. Price: $33,000.

■ With its Pentium chips, Intel cemented its dominance of the personal-computer market. Now, with the next-generation Pentium Pro, Intel goes for the server and workstation market.



■ Can the revamped Ford Taurus get it in gear in 1996? The sedan's undulating styling and stiff price (close to $20,000) scared off lots of tire kickers in 1995. Will Ford Motor make it worth their while to give the new Taurus a try?

INDUSTRY C

■ While business can't expect to sail effortlessly through the year, 1996 should turn in a better performance than '95

On medieval maps, the *terra incognita* around the borders was festooned with whirlpools, dragons, and dire warnings: "Here there be monsters!" In 1996, as the U.S. economy sails into uncharted waters, its map might well be decorated with cherubs and zephyrs. Refreshed after 1995's slowdown and wafted along by falling interest rates, American business should glide into 1996, leaving in its wake steady if not sparkling growth through the sixth year of expansion.

Favorable portents abound. Congress and the White House seem certain to deliver a plan to whack hundreds of billions out of federal deficits over the last half of the '90s. Even with the budget unresolved, the Federal Reserve cut short-term interest rates on Dec. 19 from 5.75% to 5.5%—the first of three 25-basis-point cuts that Fed-watchers expect by the end of 1996. That's welcome news: "We'll see growth in '96, but I think we'll see more of it if the Fed keeps lowering rates," says Ross J. Centanni, president of air-compressor maker Gardner Denver Machinery Inc.

Coupled with continued low inflation, the Fed's easing will ratify the remarkable rally in bond prices, keeping crucial long-term rates down. That will provide a lift to housing and commercial real estate. And America's top trading partners should struggle out of their 1995 doldrums and buy more from U.S. manufacturers.

SCROOGES GALORE. That's not to say that business will sail effortlessly through the year. The 23 industries profiled by BUSINESS WEEK in this year's Industry Outlook will need skillful navigation to steer through shifting currents. The sectors that will lead the way through 1996 will either enjoy continuing strong demand—such as semiconductor makers or Wall Street's securities houses—or, like defense manufacturers, will continue to squeeze more profits out of shrinking sales.

LEADERS

High-tech and service industries will set the pace in 1996

SEMICONDUCTORS Good-bye to boom-and-bust cycles as chips become all-pervasive

SECURITIES Continued low interest rates will fuel Wall Street

BUSINESS SERVICES The world wants American services, from advertising to consulting

SOFTWARE With the Internet, the software industry once again reinvents itself

DEFENSE Revenue keeps shrinking, but the sector is profiting from consolidation

Laggards will find themselves on the wro side of 1996's negative trends: slower growth capital spending, pressure on pricing, and tig fisted consumers. After a three-year mode ization binge with 12%-plus growth rates capital spending, investment in produce durable equipment will rise only 6% in 1996, ter adjustment for inflation. Even comput makers will lose some altitude, with inflatio adjusted sales rising 18% in 1996, vs. 27. growth in 1995, according to foreca by DRI/McGraw-Hill.

The '90s efficiency boo will spell trouble for any p ducer trying to raise pric in 1996. In a BUSINE WEEK/Harris Executive P in December (page 76), o 40% of the executives su veyed predict they will ra prices in 1996, down fr the 63% who were confide of price hikes before 19 began. "We're in a buye market," says Bradford Hildebrandt, a manageme consultant to law firms. A carmakers, restaurateurs, r tailers, and other business catering to consumers w find they're dealing wi wary customers, thanks debt burdens that have a record 19% of disposab income. "Debt is putting lot of pressure on household particularly the under-$50,0 families" who are the core of the mass mark says economist Mark M. Zandi of forecaste Regional Financial Associates.

But even careful consumers will spend enou to keep the economy growing. Jobs and incor will keep rising, and inflation will stay low, wi consumer prices up about 2.9%. That will he keep long-term interest rates near their low 19 levels, with yields on the 30-year Treasury bo averaging 6.3% for 1996. All told, BUSINESS WE expects the economy to turn in a better perfo mance in 1996 than 1995: The gross domest product will grow about 2.3%, after inflatio from the fourth quarter of 1995 to the end 1996. That's up from the 2% expected when t books are closed on 1995 (charts, pages 74, 74A

JTLOOK

That 2.3% growth may not sound like much, t, remember, the scale for measuring the nomy is changing. The Commerce Dept. is justing the way it calculates growth in GDP—particular, how much of growth represents a l increase in output vs. how much results m inflation. The old system tended to eremphasize growth in surging industries h falling prices, primarily computers, thus looning the economy's overall growth rate. The new "chain-weighted" measures will re-t price changes more quickly, resulting in s exaggeration of fast-wing sectors. So while the scale measured GDP wing at a respectable % in 1995, the Commerce pt. will probably report a gain by the new mea-es—forcing business and nomists to recalibrate no-ns of what constitutes a eak" or "strong" economy. SINESS WEEK uses the in-weighted system in s report.

OWING SEASON. However measure it, the 1996 nomy will feature some iliar trends, such as vnsizing. Outplacement cialists Challenger Gray Christmas Inc. predict t corporate layoffs will to-420,000 in 1996, matching 5's level. Payroll-shedding be most common in in-tries where the government's role, either a purchaser or a regulator, is shrinking: de-se, aerospace, telecommunications, banking, utilities.

Slash-and-burn alone, however, will no longer minate strategy sessions. "Very few compa-s have created sustainable advantages ough shrinking," says Thomas J. Tierney, naging director of consultants Bain & Co. re companies say they're focusing on growth ategies designed to increase sales, boost mar-share, and expand overseas. In a September vey of senior planning executives at 100 ge U. S. corporations, 73% said that boosting enues would be more important than cutting s over the next three years, according to the Futures Group Inc., strategic planning consultants. Only 18% of the executives surveyed emphasized belt-tightening.

One of the fastest routes to growth is acquisition. The 1995 merger boom will keep rolling—whether it's telephone and media giants scrambling for stronger positions in explosive communications markets or doctors banding together for clout to deal with insurers. Defense contractors, electric utilities, drugmakers, and banks are all feeling the heat. "People realize they need scale to compete—and it's easier to buy than to build," says mergers and acquisitions expert Kim Fennebresque, managing director of Union Bank of Switzerland. "If you have scale, you can reduce costs."

Take Union Pacific Corp., awaiting government approval for its $3.9 billion purchase of Southern Pacific Rail Corp. Ronald J. Burns, CEO of Union Pacific Railroad Co., figures the combined lines will reap nearly $700 million a year in cost savings and increased revenues when the deal is digested. With economies like that within reach, Securities Data Co. expects 1996's M&A activity to top the record $442 billion in 1995 deals reported as of Dec. 18.

Internal investment will remain heavy, too. For some industries, even a three-year boom in capital spending hasn't satisfied the need for more production capacity: Semiconductor makers are scrambling to build enough clean rooms to keep up with 20%-plus growth in chip demand. Even sectors with plenty of new facilities must upgrade for global competition. "When you're in a harsh, competitive environment, you can't stop modernizing," says Roger E. Brinner, DRI chief economist. Pharmaceutical firms, which boosted research spending by a relatively low 8% in 1995, plan to beef up budgets in search of blockbuster drugs.

Steel is an example of the modernization drive. Despite 1995's collapse in prices, steelmakers are rushing to build minimills. While

LAGGARDS

Basic industries and others serving strapped consumers will trudge along

AUTOS Sales may rise a bit, but affordability remains a nagging problem

INSURANCE Look for more mergers—and more competition for household savings

RETAILING Heavy discounting will squeeze profits as the weak disappear

METALS New steelmaking capacity will drag prices down

FOOD Supermarkets will lose "share of stomach" to take-out joints

BASIC INDUSTRIES
PAGE 81

HIGH TECHNOLOGY
PAGE 91

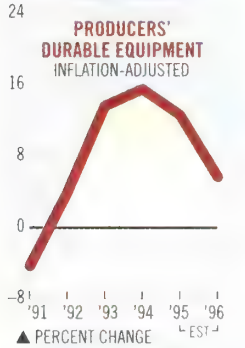
SERVICES
PAGE 99

FINANCES
PAGE 109

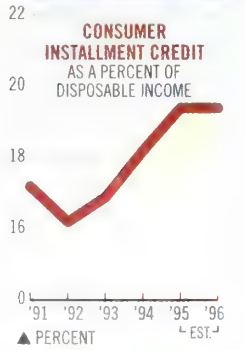
THE 1996 ECONOMY

The U.S. economy should grow 2.3%, up from 2% in 1995. Low inflation and interest rates, coupled with gains in exports, will provide the power.

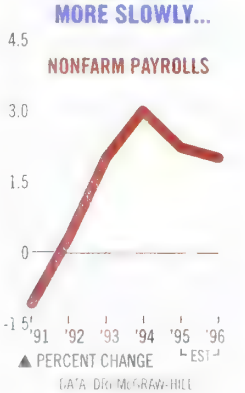
BUSINESS INVESTMENT WILL SLOW...



...AND DEBT WILL SQUEEZE CONSUMERS...



...AS JOBS GROW MORE SLOWLY...



each new minimill wreaks havoc on existing producers, cheaper production gives steel an edge over other materials: Builders, for example, are using more steel and less concrete. "People say steel demand is inelastic," says Nucor Corp. Chairman F. Kenneth Iverson. "But when you drop the price, you expand the market."

Many industries will be looking abroad to expand their markets in 1996. "We're not planning on the U.S. economy to carry us in 1996," says Daniel J. Meyer, CEO of Cincinnati Milacron Inc. Outfits such as Milacron looking to expand sales abroad can count two strong pluses in 1996: American industry is now ranked the world's most competitive, according to the Swiss-based World Economic Forum. And America's top trading partners, after a poor-to-disastrous 1995, see better economies ahead.

The biggest surprise may be Japan. After a 33% surge in the Nikkei stock index, coupled with the Bank of Japan's success at stabilizing the yen at around 100 to the dollar, Tokyo pundits are hopeful that economic stagnation will finally end after four flat years. Forecasters expect Japan's GDP to grow by 1.2% or more in 1996, after inflation.

That growth should open up possibilities for U.S. exporters. American brands are increasingly popular in Tokyo's Ginza, where Gap Inc. recently opened a store to push its low-key apparel. U.S. computer makers hold about 30% of Japan's $9 billion PC market, with Compaq Computer Corp. and IBM expecting to reap even more sales from the recent rollout of a Japanese version of Windows 95. Even American carmakers are pushing at the gates in hopes of capitalizing on last summer's U.S.-Japan trade deal: Ford Motor Co. and Chrysler Corp. unveiled right-hand-drive models of the Taurus and Neon at this fall's Tokyo auto show.

RECOVERING PESO. The other sick economy of 1995—Mexico—will also show signs of health. Following last winter's peso crisis, the Mexican economy has shrunk by at least 7%. U.S. exports to Mexico fell by 9% in 1995, while the cheap peso powered a sharp 30% rise in Mexican sales to El Norte. Now, Mexico seems set for a slow recovery, with 1.5% to 2% growth in 1996 followed by 4% or more in 1997. That won't ignite a boom in U.S. export sales, but pressure on the trade imbalance could ease if the peso gains strength against the dollar.

U.S. companies account for the bulk of the $6.3 billion in direct investments in Mexico pledged for 1996. AT&T, MCI Communications, and Bell Atlantic are spending heavily to prepare for the 1997 opening of telecommunications. Privatization will spread to petrochemical plants and railroads in 1996, and Mexico is encouraging foreigners to invest in natural-gas distribution and power plants. U.S. corporations increasingly see Mexico as an attractive production base for sales to the rest of Latin America. "We can tie together manufacturing in the U.S. and Mexico and get after markets in South America," says Kenneth C. Brown, president of GE de México.

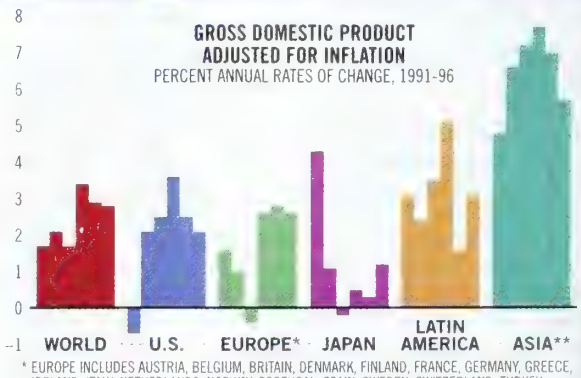
Forecasters don't expect much help with the trade balance from Canada's rebounding economy, which the Bank of Montreal predicts will grow 3.5% in 1996. With the weak Canadian dollar (trading at around U.S. 73¢) and with shaky Canadian consumers holding on to their wallets, Canada's southbound exports may grow faster than the flow of goods northward. That

PUSH COMES TO...COOPERATION

With depressingly stable prices, how do you turn a buck these days in the oil patch? Talk rivals into teaming up on production (page 87)

WORLD GROWTH

Recoveries in Japan and Mexico will lift U.S. exports in 1996. Asia will remain the world growth leader.



* EUROPE INCLUDES AUSTRIA, BELGIUM, BRITAIN, DENMARK, FINLAND, FRANCE, GERMANY, GREECE, IRELAND, ITALY, NETHERLANDS, NORWAY, PORTUGAL, SPAIN, SWEDEN, SWITZERLAND, TURKEY

** ASIA INCLUDES AUSTRALIA, CHINA, HONG KONG, INDONESIA, INDIA, KOREA, MALAYSIA, NEW ZEALAND, PHILIPPINES, SINGAPORE, TAIWAN, THAILAND.

DATA DRI/McGRAW-HILL

HOPPERS AND WOOFERS TO GO

you can sell burgers in a home-electronics ore, why not? Here, too, the name of the me is reduced overhead (page 105)

ld push Canada's merchandise trade surplus th the U.S. to a record $27 billion in 1996, s Sherry Cooper, chief economist at Toronto kerage Nesbitt Burns.

Europe may not do much for the U.S. trade ance in 1996, either. While members of the ropean Union recently unveiled their pro-sed unified currency, the Euro, the recent ench strikes to protest budget-cutting in ris highlight the difficulty that EU members l have in meeting the stringent fiscal re-irements for monetary union. French fore-ters expect growth of only 1% in 1996. Ger-ny is healthier, but business there is uggling to remain competitive in the face of h wages and taxes. "Europe still has the n and agony of downsizing and restructuring ead of it," says Nariman Behravesh, DRI's ef international economist, who predicts 2.3% wth for the EU in 1996.

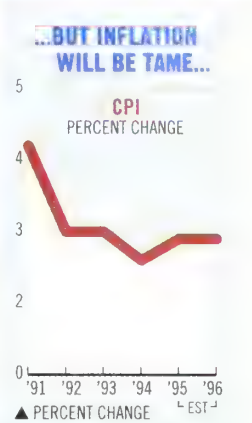
For fast growth, U.S. exporters will once in have to turn to Asia. The economies of ina, Hong Kong, Indonesia, Malaysia, Singa-e, Taiwan, and Thailand will grow at rates between 5% and 9% in 1996, down just slightly from 1995. Texas Instruments Inc., for instance, has an Asian export winner in its high-end digital-signal processing chips, made in America and sold for use in interactive toys, telecom gear, and video devices. TI's Asian sales rose 50% in 1996, says Victor Koh, managing director for Hong Kong and China, in part because Asians are buying more electronics for their own use. "We're benefiting from the higher affluence in Asia," he says.

Global crosscurrents will make 1996 the third strong year for American exports, which should grow a further 9% after adjustment for inflation. At the same time, subdued U.S. consumers may cut down on their purchases of goods made abroad. So while the U.S. will still run a trade deficit, the improved trade balance should add some $18 billion to GDP in 1996, says Allen Sinai, chief economist at Lehman Brothers Inc., marking "the first time this decade that net exports have been a plus for U.S. growth rather than a drag."

BETTER THINGS TO DO. Export gains, continued capital spending, low inflation, and falling interest rates—what could go wrong with this picture? The biggest threat to the serene economy of 1996 may lie in Washington. In their struggle over balancing the budget, President Clinton and congressional Republicans have already shut down major portions of the federal government twice and spooked the markets.

Still, neither the White House nor Capitol Hill has much to gain from a budget stalemate. For both sides, the best course is to strike a deal and move on to matters closer to politicians' hearts—such as campaigning for November's elections. If Washington's dragons and sea serpents will just get out of the way, the U.S. economy could enjoy fair winds in 1996.

By Mike McNamee in Washington, with Richard A. Melcher in Chicago, Elisabeth Malkin in Mexico City, Wendy Zellner in Dallas, and bureau reports



COMMENTARY

JOHN DEWEY, MEET PETER DRUCKER

Your revenues are rising, but not as fast as the cost of serving customers. Labor costs are climbing, but antiquated work rules and poor morale limit your flexibility. Your overseas competitors pay more, spend lavishly on training, and get far better results. Your physical plant is crumbling. Computers are scarce. And your customers are dissatisfied.

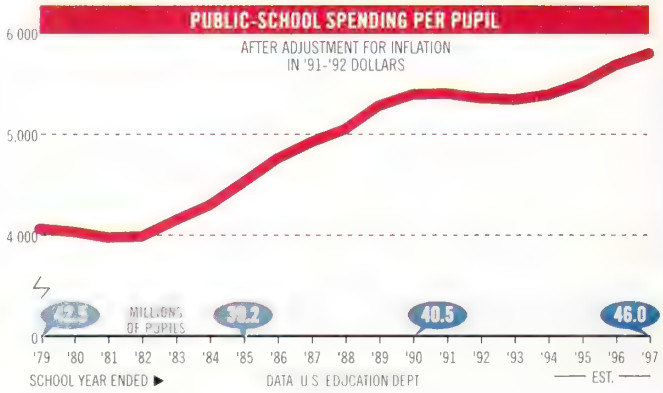
Welcome to America's public school system. Its problems are so profound and its disorganization so pervasive that it would be a challenge to the savviest of America's business managers. Just for starters: There is no central management—only 16,000 local school districts run by amateur boards pursuing their own agendas: football, creationism, condom distribution.

The school-board situation isn't going to change anytime soon, since local control is considered an inalienable right in America. But some help for what ails the schools is on the way, thanks to contemporary management theory. Two related movements—toward school choice and school standards—have far more to do with Peter F. Drucker than with John Dewey.

SURVIVAL OF THE FITTEST. School-choice advocates hope to foster competition among schools. That way, the weakest schools will lose students and either improve or fold. The strongest schools will prosper and expand. One plan would offer vouchers for purchasing education from existing private and public schools. Vouchers are strongly opposed by teachers' unions and the Clinton Administration. They argue that some kids will be left in bad schools and some schools will use the wrong lures—such as lavish spending on sports. Still, Republicans will give school choice a boost if their numbers increase in state legislatures this year.

Other reformers favor charter schools that contract to provide education to willing public-school students. Often operating out of storefronts or underused public buildings and free of bureaucracy, charter schools are generally cost-effective. These schools must demonstrate results or lose their charters. There are some 245 of them in 19 states. "This is just applying America's entrepreneurial spirit to the school," says Joseph Nathan, director of the Center for School Change, a research group in Minnesota that is tracking the trend.

K-12 SPENDING PER PUPIL KEEPS RISING



> First you decide what students should learn. Then you hold teachers and administrators accountable

Curriculum reform based on setting universal standards of knowledge is progressing much faster. It is based on sound business principles: First you decide what students should learn, and then you hold teachers and administrators accountable. "In states where they take standards seriously, they have seemed to make a difference," says Marc Tucker, president of the National Center on Education and the Economy, which helps schools in the standards effort. Critics complain that teachers will concentrate on drilling students to pass tests instead of pursuing broader educational objectives. Still, parents seem to like the results. In their second year of a standards-based curriculum, Maryland students boosted their scores by 25%.

Pressure for schools to become more efficient is intense. Immigration is swelling enrollments. The number of students with limited proficiency in English jumped by 26% during the 1980s. And children who require special education increased by 15% over the past decade. "We've got a whole influx of kids who have been exposed to alcohol and drugs, hurt by environmental contaminants, or diagnosed with learning difficulties," says Kathy Christie, a Denver-area school board member and an analyst at the Education Commission of the States.

FALLING BEHIND. All this is happening as an unpaid bill for neglect of school buildings is coming due. One-third of America's schools, serving some 14 million students, require extensive repair or replacement, according to a 1995 report by the General Accounting Office. A quarter of all public schools lack sufficient computers, and 42% have inadequate science laboratories, says the GAO.

That is a lot for local school boards to deal with. Without a clear focus on educational goals, they tend to "pay too much attention to asbestos and not enough to training teachers and developing curriculum," says Bruce Alberts, president of the National Academy of Sciences. American science scholarship in grade school is falling behind because much of the industrialized world pays "enormously more attention to teacher refresher courses and to professional development," says Alberts.

America's management gurus may not have the whole solution. But the notion that schools must measure and improve their output—graduates who can read and do math—can only help.

By Paul Magnusson in Washington

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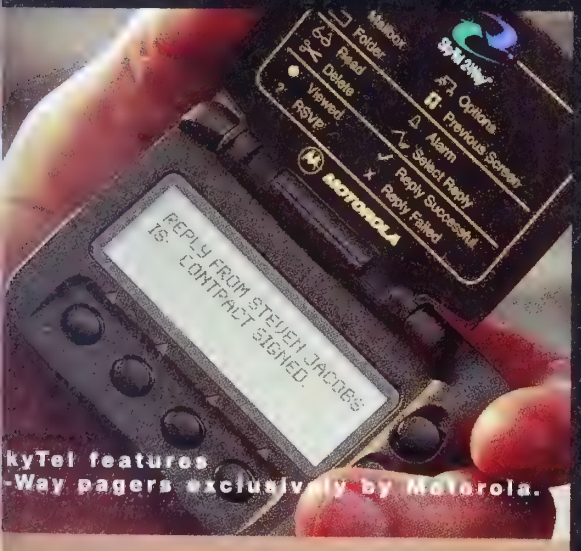

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BUSINESS WEEK/HARRIS EXECUTIVE POLL

A TOUGH YEAR TO FOLLOW

Executives at America's largest public companies see the economy cooling a bit in the coming year. They're a tad less optimistic than they were this time last year. Fewer expect growth in gross domestic product to pick up in 1996, and the number anticipating rising unemployment has doubled. But managers cheer the Fed: Their inflation fears have all but vanished, and few worry about rising interest rates. A remarkable 91% give Fed Chairman Alan Greenspan high marks, compared with the 26% who applaud Clinton's handling of the economy.

OPTIMISTIC VOICES

Overall, how would you characterize your outlook for the U.S. economy in the next 12 months—would you say you are very optimistic, somewhat optimistic, somewhat pessimistic, or very pessimistic?

	1995	1994	1993
Very optimistic	8%	13%	3%
Somewhat optimistic	78%	76%	80%
Somewhat pessimistic	13%	11%	16%
Very pessimistic	0%	0%	1%
Not sure	1%	0%	0%

GROWTH FACTOR

Compared with the last 12 months, do you think the rate of growth of the gross domestic product will go up, go down, or stay the same over the next 12 months?

	1995	1994	1993
Go up	30%	38%	25%
Go down	25%	26%	9%
Stay the same	45%	36%	65%
Not sure	0%	0%	1%

WHAT ABOUT INFLATION?

Compared with the last 12 months, do you think the rate of inflation, based on the CPI, will go up, go down, or stay the same over the next 12 months?

	1995	1994	1993
Go up	12%	53%	40%
Go down	15%	6%	5%
Stay the same	73%	40%	55%
Not sure	0%	1%	0%

TRACKING TREASURIES

Compared with where it is right now, do you think the 30-year Treasury rate will go up, go down, or stay the same over the next 12 months?

	1995	1994	1993
Go up	24%	57%	67%
Go down	47%	18%	5%
Stay the same	25%	24%	27%
Not sure	4%	1%	1%

THE JOBLESS RATE

Compared with the last 12 months, do you think the unemployment rate will go up, go down, or stay the same over the next 12 months?

	1995	1994	1993
Go up	35%	17%	21%
Go down	15%	33%	34%
Stay the same	49%	50%	44%
Not sure	1%	0%	1%

THE COMPANY WAY

And now some questions about your expectations for your company over the next 12 months. Please give your best estimate. Do you think each of the following will increase or decrease between now and December, 1996?

	INCREASE	DECREASE	SAME	NOT SURE
Sales	89%	4%	5%	2%
Wage and salary rates	85%	3%	10%	2%
Investment in plant and equipment	72%	12%	13%	3%
Health-care costs per employee	59%	22%	17%	2%
Investment in research & development	58%	14%	21%	7%
Exports	54%	3%	10%	33%
Full-time employees	45%	30%	23%	2%
Typical prices of standard products or services	40%	21%	37%	2%

PROPHESIZING PROFITS

Do you think your company's profitability will improve, stay the same, or get worse in 1996?

Improve	79%	Get worse	6%
Stay the same	13%	Not sure	2%

CRAZY FOR ALAN...

How would you rate the job Alan Greenspan and the Federal Reserve are doing — excellent, pretty good, only fair, or poor?

	1995	1994
Excellent	40%	16%
Pretty good	51%	50%
Only fair	8%	29%
Poor	0%	5%
Not sure	1%	0%

...BUT LESS SO FOR BILL

How do you rate President Clinton's handling of the economy — excellent, pretty good, only fair, or poor?

Excellent	1%	Poor	18%
Pretty good	25%	Not sure	1%
Only fair	55%		

Edited by Mark N. Vamos

Survey of 401 senior executives drawn from the BUSINESS WEEK 1000. Interviews were conducted for BUSINESS WEEK Nov. 30–Dec. 15, 1995 by Louis Harris & Associates Inc. Previous surveys cited were of 400 senior executives on Nov. 28–Dec. 5, 1994 and of 402 senior executives Dec. 10–20, 1993.

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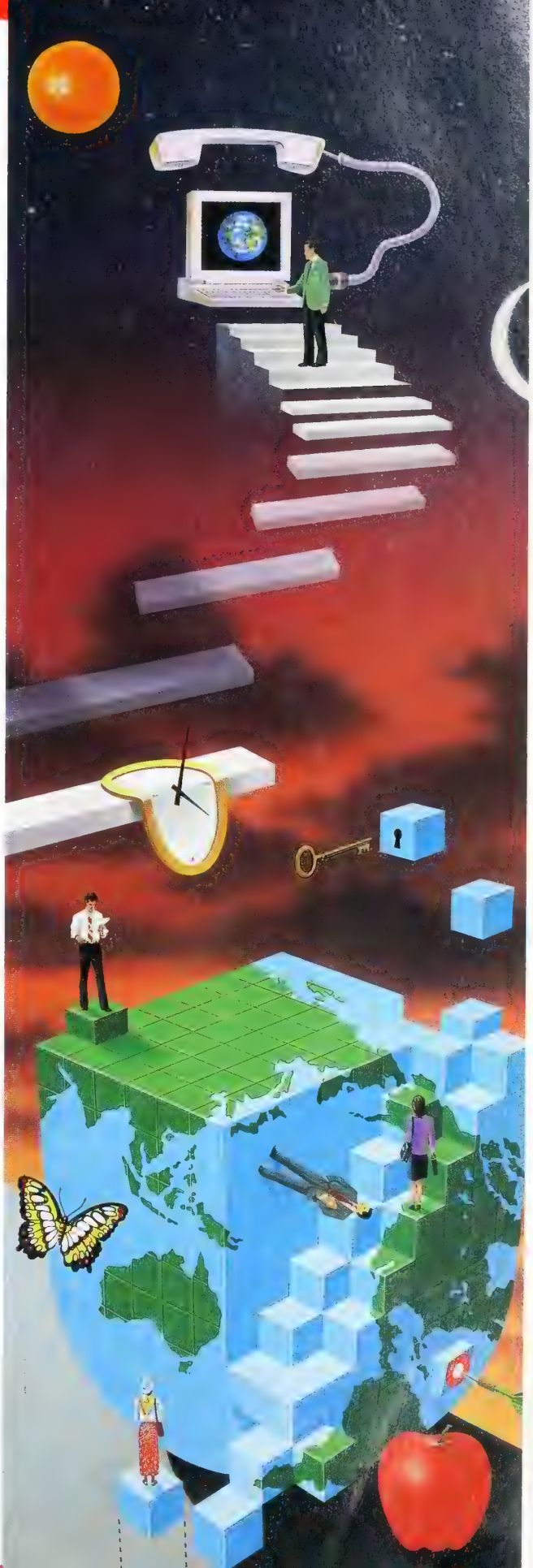
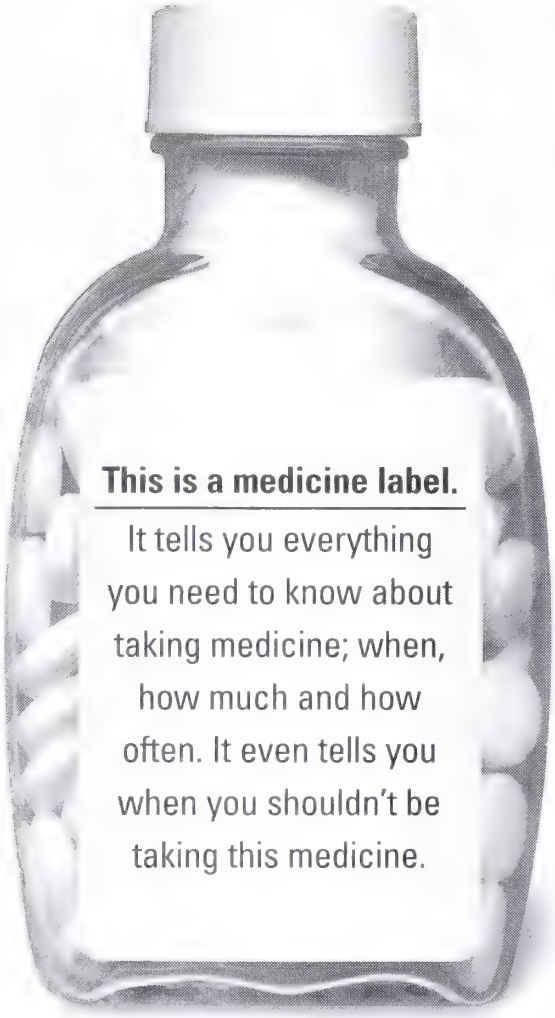


The Medicine Label... Your Road Map to Good Health



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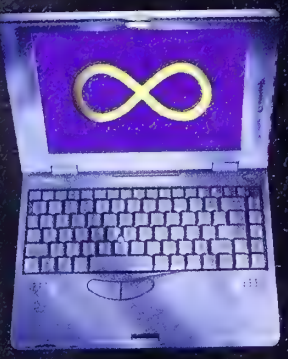

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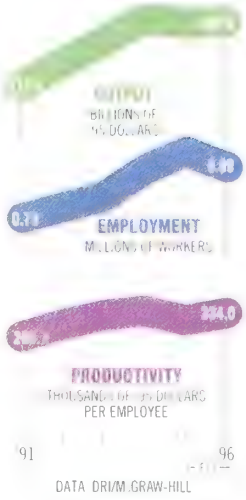
ILLUSTRATIONS BY EDMUND GUY

CRUISE CONTROL?

CAR SALES SHOULD REMAIN STRONG, THOUGH HIGH STICKER PRICES ARE WORRISOME

PROGNOSIS '96

MOTOR VEHICLES



POSITIVES

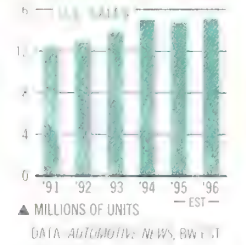
- Lower interest rates make auto loan and lease payments more affordable.
- A flood of products—Ford's Escort and new pickup and GM's family sedans—should whet consumer appetites.

NEGATIVES

- Cost-cutting and a weaker yen are making the Japanese tougher competitors than ever.
- Price-conscious consumers are demanding deals.

SPOTLIGHT

CARS/LIGHT TRUCKS



Peter Dirisamer may not drive home a new car in 1996. Dirisamer, 37, an Elmhurst (Ill.) technical writer, wants to replace his family's 1988 Plymouth Horizon subcompact. But with average new-car prices pushing $20,000, he's not finding much he can afford. "Detroit expects me to pay $20,000 for the average four-door sedan?" he sniffs. "I don't think so." Instead, he may settle for a used car.

Consumers such as Dirisamer are the reason Detroit is cautious about its prospects for the new year. "Price is the issue with customers," says Lehman Brothers Inc. analyst Joseph Phillippi. And with a flood of two- and three-year-old cars and trucks coming back on the market as their leases expire—2.3 million in 1996 alone, according to Art Spinella of CNW Marketing/Research in Bandon, Ore.—consumers are finding plenty of alternatives to pricey new wheels.

So Detroit is prepared to idle along at about the same rate as the overall economy. Auto executives are looking for only a modest improvement of less than 2% over 1995's U.S. sales of 14.8 million cars and light trucks. Says General Motors Corp. Chairman John F. Smith Jr.: "1996 looks like a good year, not spectacular."

Perhaps, too, Detroit is a bit cautious about predicting rosy sales. A year ago, its optimism had reached fever pitch. But by mid-January, consumers began to cool on auto buying as they felt the cumulative effect of interest-rate hikes by the Federal Reserve. Sales revived by fits and starts through 1995, ending about 2.6% behind 1994's pace.

GOOD AS IT GETS? Auto sales should be helped in 1996 by low interest rates, which make auto loans and lease terms more attractive. A continuing appetite for American-made trucks, including minivans and sport utilities, also is in Detroit's favor. And the Big Three are introducing a host of new models, notably Ford's Escort small car and F-series pickup, GM's new midsize cars and minivans, and Chrysler's Dodge Dakota pickup.

Still, other worries loom. PaineWebber Inc. analyst Michael Ward frets about unsold cars and trucks on dealer lots, which reached a 75-day average supply late in 1995, 14% above year-ago levels. Ward predicts little change in sales for 1996: "This is as good as it's going to get for Detroit."

While most on Wall Street predict slightly stronger sales ahead, they don't expect them flow straight to the bottom line. Customers demanding cash rebates and sweet lease te on all but the hottest-selling trucks. Fleming (N.J.) car dealer Steve Kalafer, who owns dealerships, says the only thing selling th days is bargains: "In a world full of wonde products, the consumer is buying the deal."

That squeezes auto makers' profit marg "The industry's margins are a disaster for

expansion," says P Ballew, chief economist for J Power & Associates Inc. Adding to the unc tainty, Detroit's contracts with the United A Workers expire in September. A spirited bate is expected about the auto makers' shift jobs to outside suppliers (box). And Japan competitors are hard on Detroit's bumper: int ducing snazzy new vehicles while keeping pr increases small.

Ford's costs of launching its many new v cles will continue to drag down profits dur the first half of the year, company executi say. Stockholders remain anxious about the c pany's strategy of loading on features to lure port-loving baby boomers at a time when c sumers shun higher sticker prices. Ford a will expand its ambitious global reorganizatio dubbed Ford 2000—by folding South Amer New Zealand, Australia, and Taiwan into combined North American and European ope tions in 1996. J.P. Morgan & Co. analyst Da Bradley expects Ford to earn $3.6 billion, changed from 1995, on sales of $123 billion.

General Motors Corp., which sat out m of 1995 without new models, launches a series important vehicles this year. After bungl several car launches in recent years, it has b

rking on debugging its manufacturing process prepare for the launches. GM is counting on h entries as the new Chevy Venture minivan, ick Regal, and Pontiac Grand Prix to help it gain its footing in crucial market segments. e company is hoping its falling market share ally has bottomed. Late in the year, its share ged above 34%, up from lows near 32%. GM ll earn $7 billion, up 17%, on $160 billion of es, Bradley calculates.

EAL SITUATION." Chrysler Corp. management, ich just successfully introduced a new gener- on of its bread-and-butter minivans, is likely spend plenty of time planning for a spring wdown with billionaire investor Kirk Kerkor- . If Chrysler balks at giving Kerkorian aide rome B. York a board seat, a nasty proxy ttle will ensue. Back on the plant floor, Chrys- is standardizing manufacturing processes d modernizing older factories. Bradley esti- tes 1996 Chrysler earnings of $3.1 billion, 58% from the depressed 1995 level, on sales $54 billion.

Even as Detroit rolls out spiffy new models, Japanese rivals will unveil their own new signs. And while a sky-high yen forced them boost sticker prices, putting them at a 000 to $3,000 per-car price disadvantage, ey've been slashing costs. The 1997 Toyota mry midsize sedan is expected to cost as ch as $1,000 less than the current car. "The panese manufacturers have not gone away," says GM's Smith. "They are tough competitors, and they will continue to be."

Japan also is expanding its lower-cost U.S. production—and even pping up shipments of American-built cars Japan. "We are importing, not only to Japan to 38 countries, from the U.S.," says No- iiko Kawamoto, Honda Motor Co. president and chief executive. "We intend to reinforce this plan." Even softening in the yen last fall isn't likely to cause Japan to back off from cost-cutting. Says Ford Chairman Alexander J. Trotman: "I doubt very much that they will take their foot off the pedal just because the yen has slipped back."

There is a silver lining to the slackening of 1994's breakneck pace. Back then, factories were running at maximum overtime, some key parts ran short, and demand for raw materials renewed some inflationary pressures. Says Kenneth L. Way, chairman and CEO of Lear Seating Corp. in Southfield, Mich.: "I think it's an advantage not to have deep troughs and big peaks."

Instead, the industry may be bumping along on a plateau of 14.5 million to 15.5 million unit sales annually. "It's actually an ideal situation," says Chrysler Chairman Robert J. Eaton. "It allows you to get your plants running at maximum efficiency, get your material flowing nice and evenly, and really focus on costs and quality."

And when it comes to expansion opportunities, the Big Three are casting their eyes toward the Asia-Pacific region, where they can still turn out basic cars on a shoestring. "That is where most of our growth focus will be in the next 20 years," says Ford's Trotman. Chrysler, which has lagged its Detroit peers abroad, is likely to make some major international moves this year. The company is talking with a half-dozen potential partners in India, South America, and Southeast Asia. An alliance with a European auto maker could also be in the cards.

Overseas horizons may indeed appear the brightest to Detroit. Especially if American consumers, such as Illinois car shopper Dirisamer, remain convinced that new cars cost too much.

By Kathleen Kerwin and Keith Naughton in Detroit

■ Rebates, sweet lease deals, and the cost of launching new models are squeezing margins—and the Japanese are hard on Detroit's bumper

A SHRINKING SUPPLY OF SUPPLIERS

American auto makers will rely on fewer parts suppliers in 1996. Ford Motor Co., for example, has reduced its stable from 10,000 to 2,300—and aims for 1,150 by decade's end. At the same time, Detroit has suppliers building a larger percentage of the content of its cars than ever.

What gives? The consolidation is driven by auto makers who lean on suppliers to provide entire systems for vehicles—an entire dashboard, for instance, instead of just the ashtray that goes into it. Detroit is handing off more development responsibility to suppliers, too. This favors those companies with plentiful capacity, capital, and skills. Smaller players must merge or lose the business. Some become second- or third-tier suppliers to the remaining giants.

The Big Three want global supply networks. A supplier who aspires to U.S. business in 1996 may have to be able to deliver the same parts to factories in Germany or Brazil. Among those that analysts say may grow by acquisition in 1996: Borg-Warner Automotive, Dana, and Lear Seating. Says TRW Inc. Chairman Joseph T. Gorman: "There will continue to be massive [supplier] consolidation as markets that were once national or regional become global."

Big suppliers will end up with some extra burdens. "The cost pressures on suppliers are still tremendous," says Kenneth L. Way, chairman of Lear Seating Corp. in Southfield, Mich. "You have to share engineering costs and design costs if you're a tier-one [supplier]." And auto makers keep demanding price reductions. The focus of supplier ire for 1996 is Ford purchasing chief Carlos E. Mazzorin, who wants suppliers to cut their prices by 5% a year.

Even so, Morgan Stanley & Co. analyst Stephen Volkmann projects suppliers' earnings will rise 15% to 20% in 1996. Price increases for raw materials have eased lately, he notes. Suppliers of car parts may suffer spotty slowdowns, but business in truck components should remain robust. And Japanese car companies' expansion in the U.S. provides new market opportunities for the best U.S. suppliers.

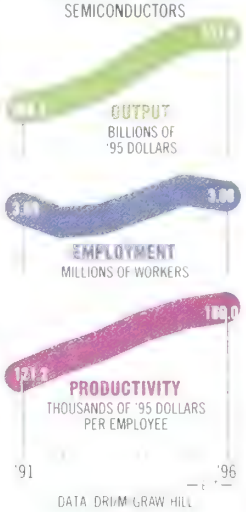
By Kathleen Kerwin and Bill Vlasic in Detroit

THEY'RE HAVING A CAPITAL TIME

SAVORING SOLID DEMAND HERE, MACHINE MAKERS ALSO ARE EXPANDING ABROAD

PROGNOSIS '96

MACHINERY
EXCLUDES COMPUTERS & SEMICONDUCTORS



POSITIVES

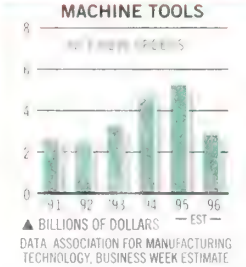
- Outsourcing by big companies means job shops will be buying equipment.
- With manufacturers concerned about global competition, they will continue placing orders for machinery.

NEGATIVES

- There's still too much worldwide capacity in sectors such as pumps and machine tools, keeping prices down.
- Automotive capital spending will flatten out in 1996.

SPOTLIGHT

MACHINE TOOLS



Business investment has powered the U.S. economic expansion, and that has made machinery executives a bunch of happy campers. Shipments of industrial machinery and equipment were up 12% through October, 1995, from a year earlier, according to the U.S. Census, surging toward a likely record. Their plump backlogs almost guarantee another strong year. Says Jeffery T. Grade, chairman of Milwaukee's Harnischfeger Industries Inc., which makes equipment for papermaking and mining: "1996, when all is said and done, will be a very good year for most industrial manufacturers."

While growth and profits won't climb much in 1996, the gains come on top of a strong base. That's because U.S. manufacturing is itself in good shape—and companies are convinced that they must invest to stay that way. "All in all, people are concerned about productivity and being competitive globally," says Daniel J. Meyer, chairman of Cincinnati Milacron Inc.

A healthy U.S. market should be supplemented by faster market growth abroad. "Our biggest opportunity for [profit] leverage is the continued accelerated growth overseas," says Thomas F. McBride, chief financial officer at Ingersoll-Rand Co. He's especially hopeful for Asia and the Pacific. Ingersoll is looking to add three joint ventures in China to the three it already has there, including one that makes industrial air compressors and another producing rock drills for mining and road-clearing. ITT Industries Inc.'s Fluid Transfer Div. is putting a warehouse for its pumps in Santiago, Chile. Milacron, which just started making small injection-molding machines in a joint venture with an outfit based in India, hopes to be producing 600 there annually within a few years.

MASS APPEAL. More machinery makers are realizing they have to intensify global activities to keep their U.S. customers happy. "When a DuPont or a Dow says, 'I'm building my next plant in China—I need you to step up your capabilities,' you've got to have mass to cover the world," says William M. Jordan, president of Duriron Co., a Dayton (Ohio) pump and valve maker. Partly with that in mind, Duriron recently bought seal maker Durametallic Corp.

Also fueling mergers—including Ingersoll-Rand's 1995 takeover of Clark Equipment Co.—is that stronger balance sheets have left more machinery makers in a position to make p chases. Indeed, there even have been some itial public offerings in the once beleaguer machine-tool business, such as a 1995 IPO Hardinge Brothers Inc., a fast-growing Elm (N.Y.) producer of lathes and machining cente

Such has been the strength of machine-t sales that the average age of U.S. metalwork equipment began falling in 1994 for the fi time in 14 years. The rejuvenation should c tinue into 1996.

Even if demand dips next year fo number of machinery makers, exist orders will provide a cushion. I instance, Alton J. Brann, cha man and CEO of Western At Inc., notes that an "exc tional year" of bookin means a good outlo for 1996 sales of its dustrial Automati Group. Its backlog machining and oth systems is up abo 50% from the $415 n lion of a year ago.

There are some strea of weakness in this rosy-hu picture. The same globalization that has U executives rushing to expand abroad mea they're facing more competition. And the sa modernization that makes American manufact ers world-beaters in productivity often has li to increases in capacity that put a damper prices.

BUYING MOOD. What's more, there are spo signs of a slowdown in demand. Manufacti ers' use of their factory capacity fell from 85. a year ago to 83.1% in November, 1995. ders for forklift trucks, industrial air compr sors, and large plastic-molding machines ha slowed in recent months. Demand from t auto industry may taper off, and 1995's slugg housing market will probably mean at best a f market for construction equipment this year

Still, most machinery customers are in a bu ing mood. Such businesses as chemicals, pap metals, and food should still spend smart Aerospace demand is finally rebounding. A one of the biggest stars is likely to be fa machinery. "The underlying fundamentals f farm equipment have never been stronge says Ted French, chief financial officer of Ca Corp., citing strong farm income and the low carryover of grain stocks in 30 years. For m chinery makers, the wheels are turning for solid 1996.

By Zachary Schiller in Clevela

METALS NEED A FEW SUPPORT BEAMS

FOR STEELMAKERS, FALLING PRICES AND LABOR ISSUES LOOM LARGE IN '96

t the dawn of 1995, Matthew Botsford, chairman of World Class Steel, was confidently raising money to build a $450 million nimill near Pittsburgh. If anyone epitomized nerica's resurgence in the steel industry, it s Botsford, an entrepreneur who had built a ccessful $20 million steel-finishing business d was following in the footsteps of Andrew rnegie.

These days, Botsford is an ex-executive. 's suing his old company—after being oust- during a November board meeting and isked from the building by a security guard. s project had the backing of banks, suppliers, d the state government. But Botsford had uble convincing equity investors—and ulti- tely his board—that a new minimill could ke money in a climate of falling steel prices. In the end, Botsford fell with a tumbling el market. In 1995, as demand dropped from l million to 110 million tons, prices plummet- too: Flat-rolled steel plunged from $440 to 5 per ton. Other products, such as structural ms, thrived. But because flat-rolled is wide- used in cars, ap- nces, and other oducts, it ac- nts for half of el sales and de- ed the year. hen we cut flat- ed prices, it was page A1 [of the per]," laments cor Corp. Presi- nt John D. Cor- ti. "When we sed prices of structurals, it was on C4."

D CARD. The industry could wind up on e one again this year, with even worse news. ecutives see unchanging demand in 1996. A er level of inventories to start the year will p avoid a replay of 1995's heavy price-cutting. t new steelmaking capacity coming onstream l put further downward pressure on prices, ecially in the commodity grades of steel. ne low end of the market is going to be gh for a while," says Roy G. Dorrence, vice- sident for operations at U.S. Steel Group.

The wild card this year is overseas. U.S. ducers hope strong growth in China will nslate into a buying binge reminiscent of 3. But the key factor for 1996 will be Eu- e. It was a vital prop under American steel ing the first half of 1995—but then buckled midyear. If a weak European economy mpts producers there to step up exports, ap European steel could undercut U.S. producers' prices and lead to fresh trade squabbles.

The biggest problem for U.S. producers is homegrown, however. Before last year's price drop, a minimill-building boom was well under way. The new mills could add 12 million tons of low-cost flat-rolled steel to production capacity in 1996 and 1997 combined. That's nearly five times the capacity added in 1995. If flat-rolled could crash last year in a relatively strong economy, what will happen to the market in a downturn, especially when new mills come onstream? "That's when we'll have our death spiral," predicts PaineWebber Inc.'s Peter Marcus, who expects lower profits in 1996 and an even greater crash later this decade.

STRIKE BAN. As if economic prospects weren't intimidating enough, labor questions loom. Most integrated companies face mid-contract wage-and-benefit negotiations in 1996. Strikes or lockouts are prohibited. But concessions granted by arbitrators could eat into earnings. Job-security clauses in these contracts limit the big mills' power to cut labor costs. Instead, the producers improve yields by tweaking the technology. In the past three years, they have added 4 million tons—the equivalent of Nucor's entire flat-rolled production—through this so-called capacity creep. Log one more factor in an eventual glut.

With a world oversupply, steel faces a dilemma just like the one U.S. aluminum makers wrestled with early in the decade. But aluminum companies, swamped with cheap Russian metal, shuttered 30% of production and negotiated an OPEC-style allotment plan. Prices recovered smartly in 1995, as massive world inventories shrank by 75%. U.S. demand rose 5%, with sales rising to 15.5 billion pounds. Aluminum looks strong again in 1996, led by a recovery in aerospace demand. But can prices remain firm if aluminum makers reopen shuttered smelters? For now, executives don't even mention the possibility, for fear of spooking the market.

In the face of such difficult markets, metal industries are more and more battling to take business away from one another. Auto hoods, tailpipes, and even beer cans are among the contentious areas. And if unexpectedly slow growth in China, Europe, or the U.S. brings about a steel glut ahead of schedule, the metal wars could grow very nasty.

By Stephen Baker in Pittsburgh

PROGNOSIS '96

PRIMARY METALS

DATA: DRI/M:GRAW-HILL

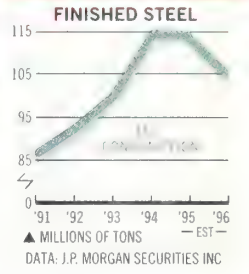
POSITIVES

- Demand for steel remains hearty.
- World inventories of aluminum have fallen 80% in the past 1½ years.
- China may return as a big customer of American steel.

NEGATIVES

- New steel capacity coming onstream is undermining prices.
- With higher aluminum prices, producers may restart idle smelters.
- Labor concessions could hurt steel earnings.

SPOTLIGHT

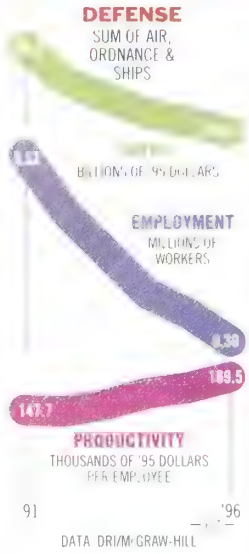


DATA: J.P. MORGAN SECURITIES INC

READY—ALL JOIN ARMS

CASH-RICH AND EAGER TO MERGE, DEFENSE COMPANIES ARE THRIVING

PROGNOSIS '96



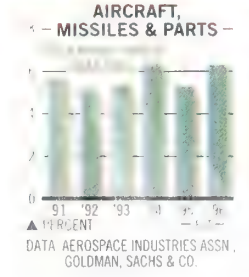
POSITIVES

- Consolidation moves forward: Look for at least one more mega-merger and continued capacity reduction.
- Modest growth in the Pentagon's procurement budget is likely, while overseas sales could strengthen.

NEGATIVES

- Profit margins will be squeezed as stingier contracts kick in. The lucrative B-2 bomber and F-22 fighter programs may be stretched or killed.

SPOTLIGHT



Financially speaking, small has been beautiful for the defense industry. For two years, defense companies have produced record profits and soaring stock prices while merging into a smaller, more efficient industry with fewer, bigger players. Year three of Operation Consolidation will bring even more mergers. "Everybody is talking to everybody," says C. Michael Armstrong, chief executive of GM Hughes Electronics Corp.

Driving the consolidation is a persistent squeeze by the Pentagon. In 1996, procurement outlays should shrink an additional 9%, to $49.7 billion—a drop of nearly 50% from the 1987 peak spending year. And despite years of contraction, the industry must still reduce capacity by as much as 40% over the next several years, according to Wolfgang Demisch, an analyst with BT Securities Corp. Arms exports will help, as the industry's share of the world market, now about 52%, should grow modestly. But the biggest gains may be logged by companies pushing forward in promising commercial ventures, some based on defense technology.

Leading the consolidation charge will be a handful of large contractors. Analysts predict at least one more merger on the scale of last year's Lockheed Martin Corp. marriage, which created a $23 billion giant. Companies have built cash hoards as a result of cutting costs even faster than the Pentagon reduced spending, leaving GM Hughes, Litton, Loral, and others poised to buy.

MARRIAGE-MINDED. Makers of missiles, electronics, and airframes are in demand. Raytheon Co. purchased the fast-growing E-Systems last year for $2.3 billion and could easily spend an additional $1 billion in 1996. GM Hughes, with some $5 billion in buying power, could swallow the defense portfolio of a TRW or a Rockwell International, each accounting for about $3 billion in annual sales. But virtually every industry sector will attract shoppers. In 1995, General Dynamics Corp. paid just $300 million for Bath Iron Works Corp. and its $2 billion shipbuilding backlog.

One megadeal, sources say, could combine Boeing Co. and McDonnell Douglas Corp. That would be a potent combination: McDonnell's $10.1 billion in government sales with Boeing's 58% stake in the world commercial plane market. It would solve each company's perennial weakness: Boeing covets military orders, such as McDonnell's recent $18 billion award for C transport planes. And McDonnell needs a c mercial partner to counter Europe's Airbus dustrie and a likely threat from upstart As competitors. Neither company will comm publicly.

While the big companies attract most of attention, the mergers-and-acquisitions ma among smaller suppliers is likely to be no lively. "The action is moving down the f chain," says Jon Kutler, principal of the Angeles-based Quarterdeck Investments.

HIGH RESOLUTION. Unfortunately for th sands of aerospace and defense work mergers will mean more layoffs. Even a cutting some 1.3 million jobs since the 1980s, the industry will shrink its workfo by an additional 30% over the next sev years, says Robert D. Paulson, a consult with McKinsey & Co. Most of the lay will come as second-tier players bail or get bought. likely candidates: U ed Technologies Co Sikorsky Aircraft Textron Inc.'s Bell H copter unit.

Conglomerates take advantage of h defense prices to load businesses to m in new directio Westinghouse Elec Corp., for instance, nounced in Decem that it will sell off defense businesses help finance its rec $5.4 billion acquisi of CBS Inc.

Entertainment and communications are ing the defense industry's greatest commer success: After surpassing 1 million subscriber its first year of operation, Hughes' DirecTV has announced plans to expand its satellite service globally. And a consortium that incl Lockheed Martin and Raytheon has inves more than $500 million to provide high-res tion satellite images to real estate agents farmers, potentially a $2 billion-plus mark

Such reassuring signs, together with the solidation craze, have Wall Street predic another year of bulging profits. BT Securi Demisch expects defense and aerospace pr to rise at least 15% in 1996, to about $5 bil Downsizing is painful, but for those who h on, the rewards can be formidable.

By Eric Schine in Los Ang

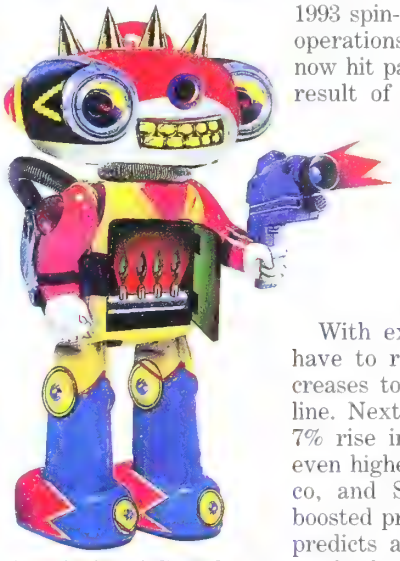
'UNEXCITING MIGHT BE GOOD'

FEW SURPRISES IN THE OIL PATCH. BUT WITH PROFITS SO HEALTHY, WHO CARES?

The oil patch has made its peace with low prices. Relentless restructuring and cost-cutting are delivering strong cash flow and ther profits despite anemic pricing. Even in lay's oil market, initial public offerings and ondary stock sales are letting small inde-ndents fund new production and property ac-sitions without incurring debt.

Executives are prepared for more of the ne in 1996. "We don't see ny things out there that k any different to us than 5," says Timothy C. Head-ton, chief executive of adington Oil Co. in Dallas, small crude-oil producer t has been steadily ex-nding with cast-offs from xon, Texaco, and others.

Most important, there's lit- evidence that prices will e a spill. Oil averaged 3.40 a barrel in 1995, and ny forecasters expect it to nain there. "I see no rea- for the 1996 numbers to nge by more than 25¢ a rel," insists Robert Gillon, ior analyst at market cher John S. Herold Inc.



at little encouragement exists is in U.S. ural-gas prices, which should recover to ut $1.80 per thousand cubic feet—up from 8 in 1995. That would put them back around 4 levels.

ADY AS SHE GOES. The major oil companies uld see their earnings rise a modest 6% in 6, thanks to a healthy economy's thirst for re oil, says Frederick P. Leuffer, senior en-y analyst at Bear, Stearns & Co. He fore-s demand growing next year by about 2%. ile hardly as robust as high tech, oils look a safe haven. "It's lackluster and sort of xciting right now," says Leuffer. "But unex-ng might be good" were the Dow to re-se course.

There are a couple of iffy assumptions in s steady-as-she-goes outlook. The biggest is t OPEC, which has suffered a steady loss of ld oil market share, continues to accept the es. Some analysts are concerned that OPEC ntries may attempt to regain share by boost-their production. Or that Iraq may return h significant new supplies. For now, neither ms likely.

Even if prices were to drop, restructuring new technology have made U.S. oil compa-s more able to cope. The best are finding fresh ways of exploring and managing. A money-saving technique pioneered by Amoco Corp. and Royal Dutch/Shell Group: pooling their assets in low-profit production regions. The two are forming a joint company to merge West Texas and New Mexico operations—and slash overlapping costs.

3-D IMAGING. Technology continues to lower costs, too (chart). Vastar Resources Inc., a 1993 spin-off of Arco's U.S. oil and gas operations, says its exploratory wells now hit pay dirt 60% of the time—as a result of technologies such as three-dimensional seismic imaging—compared with only 47% of the time using older techniques. What's more, says CEO Michael E. Wiley, "I think there will be some creative ways [cost-cutting] can continue."

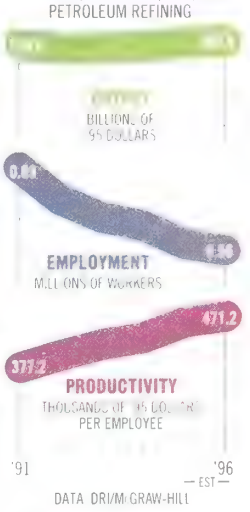
With expenses falling, prices don't have to rise much for production increases to flow straight to the bottom line. Next year's outlook is for a solid 7% rise in crude-oil production—with even higher increases for Texaco, Amoco, and Shell. Texaco, which hasn't boosted production for nearly a decade, predicts a 40% production rise within five years, thanks to rich prospects in the North Sea, Latin America, and China.

While petrochemicals were the big contributor to last year's heady profits at Phillips Petroleum Co. and Amoco, prices have softened—as supply has caught up with demand. The question now: Will China, a huge buyer that withdrew from the market in 1995, return in 1996? Bob Gower, chief executive at chemical maker Lyondell Petrochemical Co., predicts China's return could mean a second leg to the chemical boom. "All the information we have suggests we're not at the end of the cycle, but in a transition period," he says.

Retailing should continue to deliver profits, too. Continued reshuffling of gasoline outlets—as companies concentrate on specific markets—has turned the cyclical business into a reliable profit center. "We're seeing retail margins better than any time in history," says James E. Acridge, CEO of Giant Industries Inc., a Scottsdale (Ariz.) refiner and Southwest-area retailer. For years, stock analysts urged Giant to quit the business. No longer. "We're smart guys all of a sudden," he says. Stable prices and lower costs are making a lot of people look smart these days.

By Gary McWilliams in Houston

PROGNOSIS '96



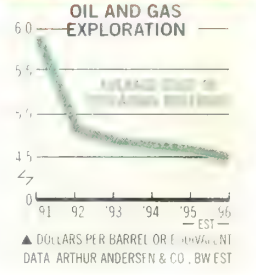
POSITIVES

- Firmer gas pricing and savings from corporate restructurings should produce stable profits.
- Advances in technology are lowering costs for exploration and drilling.
- Gasoline retailing profit margins are at historic highs.

NEGATIVES

- Petrochemical profits may soften further, cutting refining margins.
- OPEC could seek to recoup markets from non-OPEC suppliers.

SPOTLIGHT

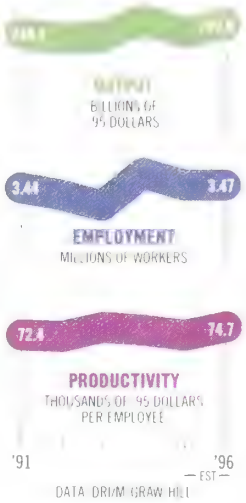


A TIME TO REAP GLOBAL REWARDS

WITH DEMAND AND OUTPUT GROWING, THE U.S. COULD AGAIN DOMINATE WORLD MARKETS

PROGNOSIS '96

AGRICULTURE



DATA: DRI/M GRAW HILL

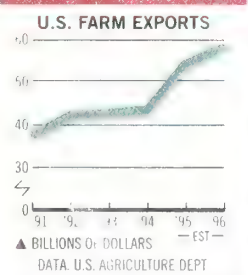
POSITIVES

- With world grain supplies at record lows and a farm bill that encourages greater production, U.S. farmers will plant fence post to fence post.
- Export demand for agricultural products will soar.

NEGATIVES

- With less government protection, farmers will be vulnerable to trade problems.
- Uncertainty over the Farm Bill could complicate planting plans.

SPOTLIGHT



DATA: U.S. AGRICULTURE DEPT

Corn and soybean farmer Robert Mullins doesn't get excited too easily. But from where he sits on an 1,800-acre spread in rural Shabbona, Ill., the export outlook is cause for celebration: "Spectacular," he says. "It's really coming alive."

The next year could bring an export bonanza for Mullins and other farmers, as U.S. agriculture begins dominating world markets again. The U.S. share of agricultural trade will rise to about 21% in 1996 after falling as low as 16.7% in 1986. The value of U.S. exports will push up to nearly $60 billion (chart), thanks to booming demand, reduced global trade barriers, and a more competitive U.S. Farm Belt. U.S. farmers have long considered exports the missing link in their pursuit of higher prices: "If Mother Nature cooperates, and we get a good crop, we could have the full package for a change," says Mullins.

In 1995, Mother Nature had other ideas. Heavy rains delayed spring planting through much of the Midwest grain belt. Two months later, a summer heat wave baked the earth rock hard. Then a killing frost in late September put a chill on the autumn harvest. With the crop stunted and plagued by disease, production of corn plunged from 10 billion bushels in 1994 to 7.3 billion in '95, sending U.S. corn stockpiles to 20-year lows. For the year, corn futures prices had soared 51% as of Dec. 14, soybeans 31%, and wheat 25%. Big rewards went to farmers who produced decent crops in spite of the weather, then held out for the best prices late in the year. But predicting such explosive rallies can be tricky: "With our reserves of feed grains at historic lows, it makes the markets more volatile," says Patrick H. Arbor, chairman of the Chicago Board of Trade.

SHRINKING SET-ASIDES. Still, the near-term trend is positive: Supplies have tightened at a time of heavy demand, especially from Asia. Spending by the Japanese, the largest importers of U.S. agricultural products, will reach $11.3 billion in 1996, up from $10.5 billion in 1995, according to projections from the U.S. Agriculture Dept. South Korea and China, benefiting from robust economies, will increase imports as well. U.S. red meat, fruit, and vegetables, along with grain, will be sought-after commodities. "We have tremendous export-market potential," says analyst David C. N son of NatWest Securities Corp. in New Yo

U.S. farmers will be planting fence post fence post this year. As of mid-December, government appeared to be all for it: Propo reforms would eliminate annual set-aside p grams that support prices by idling cropla Instead of paying farmers not to farm, the g ernment would provide fixed payments, shri ing each year, based on how much they recei in the past. With this change, the amount corn, wheat, and soybean acreage in product should jump by about 10% in the coming s son, analysts estimate. As the reforms st at the end of '95, they would have li effect on cotton, rice, sugar, pean and dairy farmers, who wo retain key subsidies.

The additional land grain crops will be a m est plus for fertilizer co panies such as IMC G bal, Freeport-McMoR and Potash. But biggest potential those companies l overseas. In China, example, average gr yields run about 50% beh those of the U.S. Yet rapid economic grov has the huge Chinese population clamoring a better diet. The simplest way to boost yiel more fertilizer. The less developed world will pouring on the potash, says Wendell F. Buec chief executive officer of IMC. "There's noth more dangerous than hungry people. You got to keep your population well-fed," he sa

Other nations' efforts to improve farm techniques won't threaten U.S. market sh right away. Greater use of fertilizer, pestici and hybrid seed, as well as increased mecha zation, could level the playing field somed But the U.S. retains a big advantage in lo cost production. And the demand is huge. C na's consumption is projected to grow even fa er than its yields. And the former Sov Union—a potentially huge competitor—has s its output crash along with the rest of its ec omy over the past five years, with no comeb in sight.

Even if the U.S. produces a bumper cr in 1996, many bins will remain empty: "We not going to be flush with supply for at le several growing seasons," predicts Daniel Basse of the AgResource consultancy in Chi go. For the rest of this decade, the world w be depending on U.S. farmers.

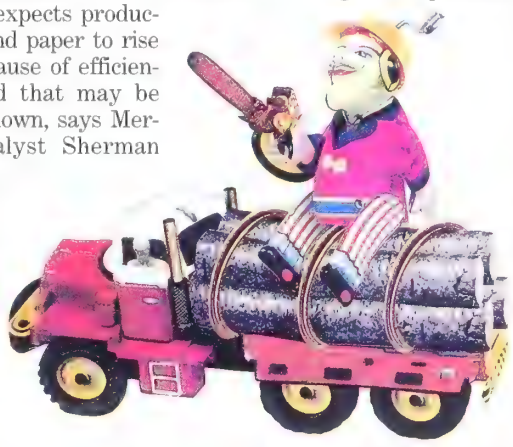
By Greg Burns in Chic

IT'S A GOOD YEAR TO GET HITCHED

'96 COULD BE TOUGH, SO PAPERMAKERS WILL CONTINUE TO MERGE

or a few crazy months early in 1995, making paper was akin to printing money. As demand outran supply, prices for white pa- took their most dramatic leap since World r II. The jump of 38% per ton in Dean Wit- Reynolds Inc.'s paper and paperboard com- ite index drove up profits an estimated 180% 1995 at the 19 largest wood and paper com- ies. As paper executives tell it, the tempta- n to add new capacity was almost unbearable. t remembering a binge that turned to bust lier in the decade, they resisted. "The mem- es are still fresh of what it feels like in a vn cycle with too much capacity," says Lynn chaelis, Weyerhaeuser Co.'s director of mar- ing and economic research.

Good thing. Fearing ever-higher prices, cus- ers stockpiled paper. By summer, the bloat- inventories undermined the sky-high prices, l they tumbled an average of 11%. Even hout big new investments, the American rest & Paper Assn. expects produc- capacity for pulp and paper to rise in 1996, largely because of efficien- improvements. And that may be ugh to push prices down, says Mer- Lynch & Co. analyst Sherman ao. Chao predicts t prices of pulp and er could decline as ch as 19% in 1996 steady volume. This lls lower profits, ugh nothing resem- ig the industry's e in the early '90s. Without any hope booming demand, ect paper and pulp companies to spend 1996 ning up balance sheets or plowing ahead h industry consolidation. "In our business, it ore favorable to buy assets than build new nts," says John A. Georges, International er Co.'s chief executive.



CTION YEAR. Acquisitions already are rolling. berly-Clark Corp. gobbled up Scott Paper for $9.4 billion in December. Earlier in the r, International Paper agreed to buy Feder- Paper Board for $3.5 billion, and paid $1.15 on for a controlling stake in Carter Holt rvey, New Zealand's largest timber-plantation ier. Boise Cascade sold its Rainy River For- Products unit to Canada's Stone-Consoli- ed and acquired a 6.4% interest in Stone. 996, look for plenty more deals, as the pow- ouses buy slices of global markets and ex- l their reach over raw materials.

As the year begins, demand for white paper is lolling at 7% below year-ago levels. Demand should recover smartly in 1996, especially in coated papers used in glossy advertising, which should be bolstered by a Presidential election and the Atlanta Olympics. "The coated grades are holding their own," says Paul C. Latta, an analyst at Ragen MacKenzie in Seattle. Newsprint, though, which climbed 40% in price from 1994 to 1995, could be headed for a fall. Inventories are at record levels, and high prices are dampening demand.

Recycling should continue to attract much of the growth in the pulp industries. Minimills, which convert old cardboard into pulp, are proliferating as such companies as Weyerhaeuser and Boise Cascade Corp. expand. Recycled materials should jump 26% in 1996, while production of marketwood pulp—the product of virgin wood chips—rises just 0.3%, according to the American Forest & Paper Assn. The extra pulp will go into producing more linerboard, kraft paper, and corrugated paper, creating a plentiful supply of those products and damping their prices, says Larry Katz of Pacific Crest Securities in Portland, Ore.

HOUSEBOUND. The lumber industry, meanwhile, is struggling against competing materials and a surge of imports. Canadian lumber now accounts for around 35% of the U.S. market, up from 28% in 1989. At the same time, growing numbers of builders are substituting steel for wood, with steel-frame housing growing from 500 to 80,000 houses in the past four years. And total housing starts will rise only modestly in 1996, to around 1.4 million. All that should spell a continued slump in lumber prices.

Meanwhile, the wood industry will press ahead with such promising engineered products as oriented strand board, a cheap new kind of fiberboard. By 1998, there should be over 7 billion feet of oriented strand board capacity, up from zero in 1988, estimates L. Pendleton Siegel, CEO of Potlatch Corp., based in San Francisco. This should claim fully 50% of the fiberboard capacity, prompting a brawl. "There's going to be a bloody market for the next two years," says Siegel. So don't be surprised to see a few of the losers get gobbled up by the industry giants.

By Seanna Browder in Seattle

PROGNOSIS '96

FOREST PRODUCTS

DATA: DRI/M-GRAW-HILL

POSITIVES

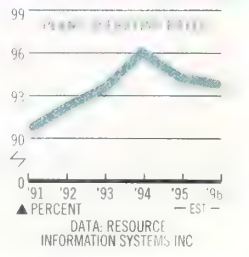
- Demand for coated paper used in advertising should be bolstered by the Presidential election and Olympic Games.
- Producers avoided bringing on fresh capacity when prices soared.

NEGATIVES

- Mills making cheap, new engineered wood products will prompt a brawl in the fiberboard market.
- The lumber industry faces intense competition from Canadian producers.

SPOTLIGHT

PAPER AND PAPERBOARD



DATA: RESOURCE INFORMATION SYSTEMS INC

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Pedro Malan
Minister of Finance

Ambassador
Luiz Felipe Lampreia
Minister of Foreign Relations

Dorothea Werneck
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HIGH TECHNOLOGY

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ILLUSTRATIONS BY PAUL WATSON

THE WEB KEEPS SPREADING

THE NEW MARKET SHOULD GROW 100% AND CREATE EVEN GREATER OPPORTUNITIES

PROGNOSIS '96

SOFTWARE & DATA PROCESSING

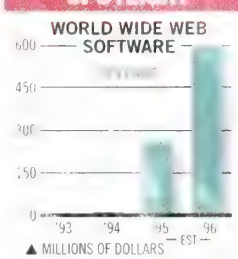
POSITIVES

- Windows 95 will spark demand for educational, entertainment, and business software.
- Businesses are rushing onto the Web, spawning markets such as digital commerce.

NEGATIVES

- Diversity in desktop software will shrink as Microsoft's clout grows and Apple's shrinks.
- Heavy discounting of software suites—and growing development costs—will make life harder for small players.

SPOTLIGHT



Netscape Navigator. Java. Yahoo. These pioneering products and services for using the World Wide Web—and their creators—stole the headlines in 1995. But Web software is still just a blip on the software radar screen. In 1996, Web-related programs—from browsers such as the Navigator to "firewalls" that protect corporate data—will be worth less than 1% of the $100 billion-plus global software market, says Hambrecht & Quist Inc. analyst J. Neil Weintraut (chart).

What the numbers don't show, however, is the subterranean shock wave the Web has sent across the software industry. Not only is the potential huge—with annual growth of 100%, sales of Internet programs could hit $4 billion in 2000, Weintraut reckons—but the rush of millions of PC users into cyberspace could change every aspect of the software business. The race to cater to cybernauts has unleashed the biggest epidemic of startup fever seen in years. And companies such as Microsoft, IBM, and Oracle are now scrambling to make the Internet part of their core strategies.

Once again, the software industry is exuberantly reinventing itself. Indeed, the Internet revolution comes as growth in other software categories is slowing. Sales of mainframe programs have been bumping along at single-digit growth rates, and Anthony Picardi, a group vice-president at International Data Corp., figures the $19.3 billion mainframe software market will grow less than 2% over the next four years, to $19.6 billion in 1999.

READY TO JUMP. The huge market for personal computer office "suites"—collections of programs that include spreadsheets, word processing, and presentation graphics programs—is also reaching saturation. But sales are poised for a 20% cyclical jump in 1996, as millions of PC users upgrade to Windows 95, predicts Goldman, Sachs & Co. analyst Rick G. Sherlund. The hottest market will remain software for so-called client-server computing—which should grow at 40%, he figures.

All told, says IDC's Picardi, the global market for packaged software—about 75% of it made in America—will grow 10% in 1996, to $102 billi The number would be bigger if not for ma frame software, which makes up nearly 20% worldwide sales. "Other industries would for a similar growth rate," Picardi says.

And what about the new "Webware"? 1995, businesses set up Web sites like periscop to see what was going on. This year, as they t with the idea of electronic commerce across t Net, many companies will start using inter Web sites as windows into their own networks creating "intranets." Says analyst Rich Edwar at Robertson, Stephe & Co. in San Franc co: "Every softwa company will have participate."

No question, tranets are comir Corporate comput managers increasing see Web pages as means to inexpensive publish and share i formation internal This is very mu what Lotus Develo ment Corp. had mind with Notes, "groupware" progra that helps teams employees share doc ments or business a plications simultaneously over a network. the Net, much of this can be done on shar Web "pages"—for a fraction of what it cos to buy, install, and customize Notes. Lotus, quired by IBM for $3 billion last summer, is riously rejiggering Notes for the Net.

Meanwhile, Web software startups—inclu ing Netscape Communications Corp.—can ca in. Companies such as Cambridge (Mass.)-bas Vermeer Technologies Inc. and OpenMarket I should do a brisk business selling software th helps companies build and maintain Web site

The Web is also driving demand for new p gramming tools such as object-oriented so ware languages. Versant Object Technology Menlo Park, Calif., ParcPlace-Digitalk in Su nyvale, Calif., and Steven P. Jobs's NEXT Co puter are tailoring their programs—which programmers build software from reusab chunks of code—to run across the Interne The upshot: Sales of object-oriented prograr should double from this year's $300 million, a cording to IDC.

This explosion of Web activity has forc most software giants to rethink their gan

ns. Microsoft Corp. is building Internet links
all of its software products, from office
es to operating systems, and the software gi-
is licensing Sun Microsystems Inc.'s Java
gramming language. IBM has also made the
ernet a priority: Big Blue has created an
ernet software unit. Oracle is offering a fam-
of Web programs, including a "browser" and
versions of its database software.

One reason industry executives and analysts
h over cyberspace: It is one of the few do-
ns where Microsoft is not dominant. A quick
at the packaged software market explains
that matters. Most of this year's growth in
e suites will go directly to Microsoft, which
s about 90% of the $3 billion market. In
ition, a large portion of multimedia CD-ROMs
this year will be Microsoft titles. Gold-
's Sherlund figures Microsoft's net will hit
billion in calendar 1996—up 20% over last
r—on sales of $8.7 billion, up 16%.

PED UP. Another place where Microsoft has
been able to dominate is client-server com-
ng. In 1996, big corporations will continue to
nsize their computer operations from main-
nes to networks of servers—usually souped-
PCs or Unix workstations—and PC "clients."
he process, they'll pump billions of dollars
client-server databases from Sybase, In-
nix, and industry leader Oracle, whose sales
jump 40% in 1996, to $4.9 billion, predicts
rlund.

licrosoft is far from discouraged in client-
er software. A server version of Windows NT
eplacing Unix on many corporate networks
the software giant expects strong sales in
6 from its long-awaited relational database
rade, called SQL Server 6.0. It is expected
sell for a fraction of the price of Oracle,
ase, and Informix programs. And, Microsoft
s to package SQL Server with other server programs, such as systems management packages, and offer the bundles at steep discounts.

Mainframe software vendors have also hopped on the client-server bandwagon. Take Computer Associates International Inc. The Islandia (N. Y.) software maker's revenue from client-server software grew 79% in the first half of 1995 from a year earlier, while mainframe software sales—still 70% of the company—grew just 18%.

Continued corporate downsizing is another boon to software makers. Having already stripped away layers of middle managers, many large companies are trying to squeeze out further efficiencies. One way is to junk disparate computer systems that run various operating units. "Integrated enterprise software," supplied by the likes of SAP, Baan, and Oracle, does the job (box). Another way to boost efficiency: automating customer support. Newly public companies such as Vantive, Clarify, and Remedy have software that creates electronic files, or "cases," from each customer query or complaint. Later, anyone in sales, marketing, or customer support can call up the entire history of the transaction. Hambrecht & Quist's Weintraut figures sales of such "customer interaction systems," roughly $400 million in 1995, could grow to $3 billion by 2000.

Merger mania swept through software in 1995 and is likely to continue in 1996. Computer Associates bought Legent, IBM bought Lotus and, in December, SoftKey International Inc. pulled off a hostile deal to take over Learning Co. On Dec. 20, Informix Corp. bid for Illustra Information Technologies. But, with the Net spawning new startups every day, for every company that gets merged out of existence, two new ones are bound to appear.

By Neil Gross, with Amy Cortese, in New York

■ Now, as well-heeled corporations start stitching the Web into their networks, startups can cash in, and software giants have to rethink their plans

YOUR DATA SHOULD MEET MY DATA

Hark back to the old days in the computer industry—about two years ago. A salesperson at Digital Equipment Corp. could drill down in a company database to fish out technical specs for a customer. But the data produced might not match what a Digital inventory manager kept separately on her desktop computer, resulting in annoying delays while users cross-checked their information.

That's why Digital and dozens of other companies are hot on so-called "integrated enterprise software." The idea is to junk all the old "legacy" systems that separately handle a large company's customer orders, inventory, shipping, and logistical information, and replace them with a single set of programs to run the company. That way, all the data look the same, regardless of who's tapping in or where they work.

Large multinationals already have installed billions of dollars' worth of these systems. This has flooded the coffers of industry leaders SAP in Germany and Baan in Holland. Americans missed the first wave, but now Oracle Corp., Microsoft Corp., and others are plunging in. The sector is poised to grow 14% worldwide, to $11.1 billion in 1996, according to International Data Corp.

The market for related services is a gold mine, too. Deloitte & Touche's consulting arm rakes in $200 million a year advising SAP customers. It's "a phenomenal success," says Darvis Cormier, a D&T international director.

Such services don't come cheap: A switchover can cost a large manufacturer $100 million, making it "the most expensive systems decision a company has ever made," says Dick J. Fishburn, chief information officer of Digital, which is installing SAP software.

And if your company buys such a system, your integration problems aren't instantly solved, warns Vinnie Mirchandani, an analyst with Gartner Group, based in Stamford, Conn. He calls enterprise systems "a 40% solution masquerading as a 100% solution." Still, a 40% solution is better than none. And that should put plenty of wind underneath the wings of software and services companies in this hot niche.

By Neil Gross in New York, with Gail Edmondson in Paris

THIS YEAR, SERVERS WILL BE KING

PCs ARE EVERYWHERE. NOW THE SPOTLIGHT IS ON MACHINES THAT CAN LINK THEM

PROGNOSIS '96

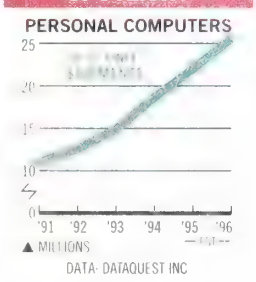
POSITIVES

- As computers get cheaper, they will become even more central to the economy.
- Electronic commerce is fueling demand for high-capacity Web servers.

NEGATIVES

- Standardized parts and designs will gnaw at the profitability of midrange and large computers.
- Personal-computer makers will feel more pressure from Intel's gradual entry into PC manufacturing.

SPOTLIGHT



For more than a decade now, the computer industry has been driven by a vision of giving everyone his or her own computer. Large organizations have rushed to put a PC onto every desktop and stopped expanding their budgets for mainframes. Engineers switched in droves from sharing minicomputers to running their own workstations. Families have scooped up millions of PCs, too, for use in home offices and to entertain the kids.

Now, with personal computers seemingly everywhere, the spotlight is shifting back to larger computers—the kind that can do work for many different people at once. Collectively known as network servers—everything from souped-up PCs selling for $10,000 to mainframes and supercomputer-class systems costing millions—big iron will be in for the most technical change and competitive action during 1996 and the following few years. "Servers are regaining their place as the fulcrum of business computing," says Gregory Garry, analyst at Dataquest Inc. "They're the centerpiece of the network."

Servers also remain the sweet spot of the computer market, offering gross margins of 30% to 50%, vs. the 15% or less seen in PCs. "Servers are clearly the healthiest segment of the computer industry," says Laura Conigliaro, computer analyst at Prudential Securities Inc. In corporations, small servers store files and move E-mail for departments. Giant servers can act as data warehouses—massive libraries of detailed product, sales, and financial information gathered from across an organization's many other computers. The World Wide Web, with close to 100,000 servers in place and hundreds more being attached every week, is also a major contributor to server demand.

PRICE-CUTTING. All told, International Data Corp. (IDC) estimates that shipments of servers based on PCs—machines using Intel chips or souped-up versions of Apple's Macintosh—will grow 35%, to 1.05 million units, from 777,000 in 1995. Shipments of servers based on proprietary hardware designs, from companies such as Hewlett-Packard Co. and Sun Microsystems Inc., will increase about 15% in 1996.

At the same time, PC sales will remain strong. Dataquest estimates that U.S. consumption of PCs in 1996 will hit 25.6 million units, up 16% from 1995 (chart). Worldwide consump will grow by 19%, to 68.7 million units. Pr cutting will stunt growth in dollar terms: reckons total U.S. spending on PCs will be only 12.6% over 1995.

The news in other categories is mixed. W station shipments are projected to grow f 847,000 units in 1995 to 982,500 units in 1 Sales of IBM-compatible mainframes will fall, f $7.5 billion in 1995 to $7.1 billion in 1996, as a of cheaper machines based on microprocess grows more popular.

THE PREFAB FOUR. Although booming, the se er market may be in for some jarring chan in 1996, thanks to Intel Corp. Along with new top-of-the-line P6, or Pentium Pro, mi processor, Intel has launched a complete cuit board containing four P6 chips. This Q P6 board is designed specifically as a build block for low-cost servers. Like the prefabri ed motherboards from Intel that helped relat ly small Packard Bell and Gateway 2000 b IBM and Compaq to market with the first P tium-based PCs, the Quad P6 board could lots of new players into the server busin overnight and change the market's econom Bottom line: Margins will begin to resem those of the cookie-cut desktop-PC market.

Intel's Quad P6 w just affect the low end the server business. Co panies such as Sequ Computer, Chen Syste and Data General plan gang as many as a doze the boards together to p duce systems that can perform traditional ma frame computers for fraction of the cost. Pai Webber Inc. computer a lyst Stephen K. Smith ures that P6-based serv will sell for less than half the price of prop tary servers at the same performance le It's "one of the most significant hardware de opments to impact the computer industry si Compaq cloned the IBM PC," he says.

Luckily for HP, Sun, and other compan making non-Intel-based servers, Quad P6-ba machines won't start shipping in volume u late 1996, and there will be a lag before s ware can be readied to take advantage them. But the warning shots have been fi for another major battle in an industry t seems to thrive on turmoil.

By John W. Verity in New Y

SILICON GOES FROM PEAK TO PEAK

IN A BOOM THAT COULD LAST A DECADE, TURNING OUT ENOUGH CHIPS IS THE BIG PROBLEM

or the companies that plant those teensy transistors on the silicon chips from which personal computers and other electronic gets sprout, 1996 shapes up as the fourth ecutive year of 20%-plus growth—26%, ac-ling to the Semiconductor Industry Assn. t's remarkable. Chipmaking has long gy-d through boom-and-bust cycles every e years or so. And while growth in 1996 't match 1995's spectacular 40% sales jump, ysts still look for chipmakers to post per-e earnings gains aver-g 29%.

he outlook is for steady vth until 2000, and per-s beyond. "There's go-to be a black hole for puting power for at t a decade," says Gor-A. Campbell, chairman artup 3Dfx Interactive , which makes chips accelerate onscreen hics for multimedia PCs. optimism isn't limited ilicon Valley entrepre-rs. Vladi Catto, chief nomist at Texas Instru-ts Inc., says the industry might expand by a year for the next two decades. By com-son, since TI made the world's first mi-hip 36 years ago, the industry has aver-l 15% annual gains.

THE ROLLER COASTER? To be sure, not y sector is booming. The growth rate for imedia PCs seems to be slowing, for exam-No matter. Most chipmakers won't be able atisfy demand anyhow unless the whole PC ness falters. "The rate at which semicon-ors are going into [a widening profusion of lucts] has just skyrocketed," says G. Dan cheson, president of chip watcher VLSI Re-rch Inc. This ever-expanding base of cus-ers means producers are becoming less vul-ible to a hiccup in any one market, adds n-Philippe Dauvin, chief economist at Eu-an chipmaker SGS-Thomson Microelectronics. t's a key reason why the industry believes oller-coaster cycles are a thing of the past. le chipmakers can't escape broad economic gs, these ups and downs will be a merry-ound ride by comparison.

ecause PCs remain the main engine boosting on's rocket for now, the immediate benefi-ies will be the makers of dynamic random-ss memory (DRAM) chips and, of course, In-Corp. New PCs gobble two to four times as h memory as older models, so DRAM ship-ments could soar 40% this year. As for Intel, look for the microprocessor king to sell 25% more "brain" chips this year than in 1995.

Despite fatter sales, Intel cautions that its incredible 55% gross margins could shrink, because of its rapidly growing business in PC motherboards and plug-in boards. On the other hand, some analysts say Intel's profits could actually improve. Its chip sales are shifting dramatically from 486 microprocessors to higher-priced Pentium models (chart), and Intel may pare prices less aggressively. That's because up-and-coming microprocessor rivals such as Cyrix and NexGen—soon to become a division of Advanced Micro Devices—aren't cranking out enough chips to cramp Intel's style. Advanced Micro Devices Inc. recently said its fourth-quarter profits would fall short because it isn't grabbing as much 486 business from Intel as it hoped.

NexGen Inc. and Cyrix Corp. are hardly the only companies facing a capacity squeeze. In fact, lack of capacity will rob the chip industry of several percentage points of potential growth this year. "Everybody's straining just to get enough fabs out," says Ray Stata, chairman of Analog Devices Inc. "Fab" is chip-speak for wafer-fabrication plant, the squeaky-clean factories that make semiconductors.

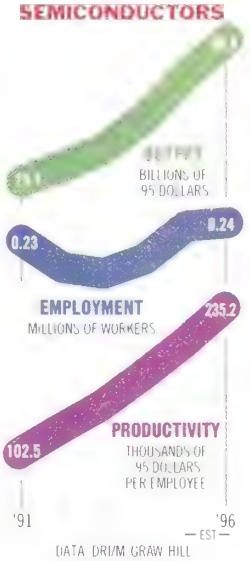
Scarce capacity means continuing pain for the fabless companies that often design the industry's leapfrog chips. To guarantee production of their next wonder circuits, several fabless companies are buying into chip producers. Cirrus Logic Inc., the biggest fabless company, plans to spend $2 billion over the next five years. Part of the money will go for a 15% stake in United Silicon, a new chip factory in Taiwan.

Wafer fabs now cost as much as $1.3 billion each, and the industry will need to pour the foundation for a new one every week, figures TI's Catto, if chips are to reach the $331 billion level predicted for 2000 by market researcher Dataquest Inc. However, until investors share the industry's newfound confidence that chips have outgrown their boom-and-bust days, the stock market could gum up Dataquest's long-range timetable. Absent that, the silicon horizon has a bright golden glow.

By Robert D. Hof in San Francisco and Otis Port in New York

PROGNOSIS '96

SEMICONDUCTORS



DATA: DRI/M GRAW HILL

POSITIVES

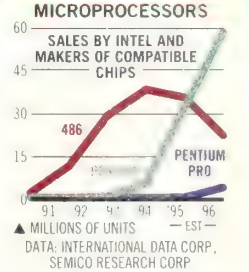
- PCs continue to boom, driving sales of memory chips and Intel's Pentium microprocessors.
- Use of chips in a growing variety of products will smooth the traditional boom-and-bust cycles.

NEGATIVES

- Capacity shortages could hurt producers of memory chips and chipmakers that contract out.
- Investor jitters about possible market slowdowns could sink stocks and limit chipmakers' investing in new plants.

SPOTLIGHT

MICROPROCESSORS



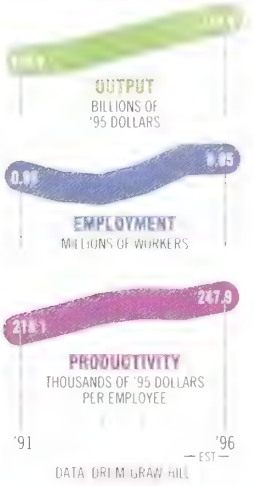
DATA: INTERNATIONAL DATA CORP., SEMICO RESEARCH CORP

THE NOT-SO-CALM BEFORE THE STORM

ALL HELL WILL BREAK LOOSE WHEN DEREGULATION HITS. FOR NOW, BUSINESS IS STRONG

PROGNOSIS '96

TELECOMMUNICATIONS
INCLUDES CABLE & OTHER COMMUNICATIONS SERVICES



DATA: DRI/McGRAW-HILL

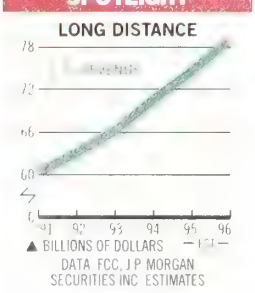
POSITIVES

- Deregulation will unleash a wave of investment and creativity.
- Demand is booming. Long-distance usage keeps rising, and households are adding second lines in record numbers.

NEGATIVES

- While deregulation is in sight, state and federal agencies must work out hundreds of details first.
- Carriers will have to spend billions of dollars to get into one another's markets.

SPOTLIGHT



DATA: FCC, J.P. MORGAN SECURITIES INC. ESTIMATES

The telecommunications industry is setting off on a great adventure in 1996: The forces of competition are being unleashed in all parts of the business for the first time. However, most of the year will be a profit-boosting calm before the storm—"the last good year before competition starts in earnest," says Simon W. Flannery, an analyst at J. P. Morgan Securities Inc. "The cable companies rolling out telephones, the Bells getting into cable, PCS [wireless] systems being switched on—all the things we're just guessing at at the moment will start coming into focus in '96."

Congress had tried for two decades to pass legislation that would overhaul the 1934 rules regulating telecommunications. Finally, at the tail end of 1995, Congress was able to write a sweeping telecom-deregulation bill that allows long-distance carriers, local phone companies, and cable-TV operators to enter one another's markets. And even without Congress, about half the states are freeing up local phone markets. By next January, competition should be busting out all over.

The telecom legislation allows long-distance and cable-TV operators into the local phone market immediately. Local monopolies can offer long distance and cable TV outside their regions at once, and in-region as soon as competition is established. If there are no hitches, Bell Atlantic Corp. Vice-Chairman James G. Cullen predicts that consumers in some parts of the country will be able to choose a local phone company by the end of 1996.

GRAB A PARTNER. As all the industry's players scramble to ready themselves for this brave new world, expect to see a flurry of alliances, partnerships, and outright acquisitions. Bell Atlantic Corp. and Nynex Corp., which have teamed up in three wireless and entertainment partnerships already, are likely to offer long-distance together as well. Analysts say other such pairings are probable. And look for buyouts of small long-distance and alternative-access companies such as WorldCom and MFS Communications.

In the meantime, business is booming. Demand for Internet access, the growth of telecommuting, the huge popularity of cellular phones, and a surge in data transmission all make telephony a growth business. Long-distance calling traffic accelerated by 8% in [illegible] and is expected to grow another 8% this [illegible] Local phone companies should add access [illegible] at a rate of 3% this year, compared with 1[illegible] 2% earlier in the decade.

The result: Phone companies are bringing money like never before. Steven R. Yanis Oppenheimer & Co. expects revenues for the three biggest long-distance carriers—AT&T, MCI Communications, and Sprint—to grow by [illegible] in 1996, to $118 billion, while the seven [illegible] Bells should see 3.2% growth in revenues, to $96 billion.

Once competition starts, price wars will break out and margins will be under pressure. [illegible] the phone companies [illegible] to start getting ready for competition now, an exhaustive task. Market researcher Forrester Research Inc. in Cambridge, Mass., predicts that the local and long-distance carriers will need to spend $30 billion over the next three years to bankroll their competitive strategies. J. P. Morgan estimates that capital spending is expected to increase to [illegible] per phone line, from $120 per line in 1995.

The local phone monopolies in particular must develop a competitive mindset. "They really need to get much more focused on customer service," says Larry R. Levitan, managing partner for Andersen Consulting's communications group. For proof, just look at a new study from Deloitte & Touche: Nearly 40% of corporate telecom managers say they would be likely to switch from their traditional local-service provider if given a choice of comparable quality. That's why industry analysts think phone companies with large rural territories and few corporate customers, such as SBC Communications Inc. and U S West Inc., are best positioned for the deregulated world, since they are the least likely to face competition.

With the Bells freed to enter new markets such as long distance and cable, deregulation should be a "win-win" for everyone in the long run, says Yanis. "I truly believe that competition will increase the size of the whole market. This will not be a zero-sum game. It's a positive-sum game." And the starting gun is about to go off.

By Catherine Arnst in New York

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ne disc is formed by back-to-back
onding of two .6mm thick, 5-inch
iscs. The track on the new DVD
Disc is finer, allowing for
4.7 gigabytes of storable
data on a single side.

This new
technology applies
to a home entertainment
product as well as a
computer storage
device.

Prototype (DVD) player is shown here. Actual product available second half of 1996. TIMM multimedia [illegible]s currently available.

The future. It's not about fear.

DVD technology will create interactive programming for business,

It will be about a rebirth of ideas and information.

education and entertainment, allowing for about seven times more data on

Immediate. Faster. And in a smaller package.

one side than your present CD or CD-ROM. Toshiba, a leader in DVD technology,

Digital compression will be the new globalspeak.

has defined the future. Prepare for the highest-quality, uninterrupted,

And like a child in the back seat, you keep asking, Are we there yet?

real-time full-motion video experience. Silicon Valley and Hollywood, here we come.

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ROBUST AND READY TO BRAWL

DRUGMAKERS ARE FLUSH, SO MORE MERGERS—EVEN HOSTILE ONES—MAY BE ON THE HORIZO

With stock prices setting records and earnings climbing at double-digit rates again, pharmaceutical executives are heading for maybe their best year since the roaring '80s. More unit sales, more freedom to raise prices, and savings from restructurings are hypercharging growth. "We're not in the doldrums of the early '90s anymore," says Robert L. Andrews, a Deloitte & Touche managing director.

Heavy margin pressure, sharp staff cuts, and deep discounting are fading as fast as memories of President Clinton's election-year attacks on drugmaker price-gouging. For 10 leading U.S. and European drugmakers, net income this year may rise as much as 12%, to $18.6 billion, while sales climb 8%, to $106.2 billion, estimates Cowen & Co. analyst Stephen Scala. The healthiest companies could repeat 1995's 20% earnings gains.

Yet execs can't afford to be complacent. Mergers have reshaped the industry, and more may be on the way. The biggest companies gain an edge in funding research and development, bargaining with managed-care buyers, and competing globally. By mid-December, the industry had tallied $41.2 billion in deals, up from 1994's record $36.1 billion, according to Windhover's directory, *1995 Health Care Strategist.*

TWISTED ARMS. Foreign buyers set the pace in 1995, led by Glaxo Holdings' record-breaking $14 billion purchase of Burroughs Wellcome, Hoechst's $7.1 billion acquisition of Marion Merrell Dow, and the stock-for-stock merger of Upjohn and Pharmacia, valued at $7 billion. Hostile deals, such as Johnson & Johnson's $1.8 billion takeover of Cordis, a maker of cardiology devices, could bring an unwilling partner or two to the altar this year. Says Brown Brothers Harriman & Co. analyst Neil B. Sweig: "The white gloves are off."

Who's next? Industry titans Bristol-Myers Squibb Co. and Eli Lilly & Co. figure prominently in Wall Street speculation as potential acquirers of the midsize likes of Monsanto Co.'s Searle & Co. unit or perennial merger target Warner-Lambert Co. Well-heeled Swiss drugmakers Ciba-Geigy Ltd. and Sandoz Ltd. also make likely buyer lists. Japanese drugmakers, whose stockholders are wrestling with tough times generally, could be alluring to global buyers.

Acquisitions aren't always the right tonic. Merck, SmithKline Beecham, and Lilly are still chasing a payoff from pharmacy-benefit managers, the distribution operations for which they together have paid $13 billion since 1993. At the same time, Rite Aid Corp. and other drugstore chains are building competing units. After shelling out $6.6 billion in 1993 for Medco Containment Services Inc., a big benefit manager, Merck & Co. has turned cool toward all kinds of mergers. Says CEO Raymond V. Gilmartin: "Major acquisitions would be a diversion for us."

STICKER SHOCK. Acquisition fever may be tempered, too, by slightly more pricing freedom. "Companies are less inclined to give discounts and reduce prices," says Wayne P. Yetter, chief executive of Astra Merck Inc. Indeed, some prices—chiefly to retail drugstore buyers not covered by insurance plans—have been climbing faster than inflation.

The industry's financial health conceals a shortfall of novel blockbusters. While drugmakers squeeze ever more sales out of big producers such as cholesterol-fighters and antidepressants, few have offered truly new potential $1 billion sellers recently. One likely exception: the osteoporosis treatment Fosamax, a drug from Italy's Istituto Gentili being marketed by Merck in the U.S. Another potential big winner is J&J's Risperdal, a schizophrenia treatment.

Drugmakers aren't helping their cause by limiting R&D. The Pharmaceutical Research & Manufacturers of America says the 8% growth in industry R&D spending in 1995 was the lowest in more than two decades. "I worry that by reducing the rate of increase in research, we are going to reduce the opportunities" for new drugs, says Schering-Plough CEO Richard J. Kogan. He says his company will outpace its peers in 1996, boosting its $650 million in R&D spending by more than 10%.

R&D cannot be neglected. Pfizer Inc. credits new drugs for boosting its net income an estimated 20% last year, to about $1.6 billion, on a 23% rise in sales, to $10.2 billion. This year, analysts expect Pfizer to nearly match that growth. Luckily for Pfizer's competitors, this won't be the year they'll have to pay for underinvestment. There's enough right with the drug business that there will be plenty of gains to go around.

By Joseph Weber in Philadelphia

PROGNOSIS '96

PHARMACEUTICAL

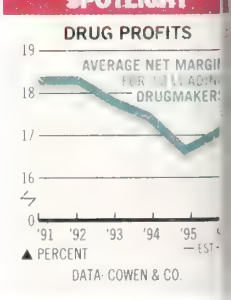
POSITIVES

- More providers are u ing medicine instead o surgery or psychothera
- Pressure against pric hikes is easing, helpin broaden profit margins
- Wider uses are being found for big sellers su as cholesterol-reducers

NEGATIVES

- With few new block- busters, drugmakers will battle to sell more of what's already in th medicine cabinet.
- Merging companies jeopardizing their futu by cutting R&D.

SPOTLIGHT



SERVICES

MEDIA/ENTERTAINMENT
The buying frenzy isn't over yet—and here comes telecom deregulation, hurling hungry new players into the arena
PAGE 100

HEALTH CARE
Despite the apparent stability, the industry is still unwieldy, fragmented, and ripe for a restructuring
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RETAILING
Not much relief for apparel chains or discounters. But sales may pick up for catalogs and department stores
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TRANSPORTATION
The worst is over for airlines, and railroads are steaming along. For truckers, gathering speed won't be such a snap
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FOOD
Consumers want it quick and easy, filling up family eateries and heating up the market for convenience foods
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High-cost power plants have long dreaded deregulation, and this is the year their worst fears may be realized
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BUSINESS SERVICES
Around the globe, there's a corporate cry for outside help—and firms will be working overtime to fill the need
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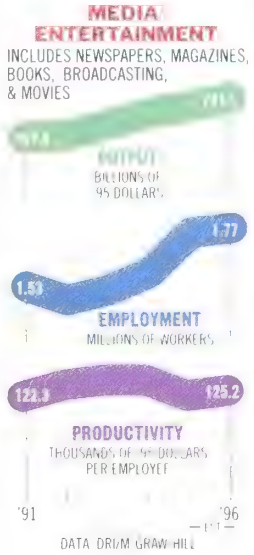
ILLUSTRATIONS BY DAVID McLIMANS

THE MEDIA CIRCUS IS STILL IN TOWN

THRILLS AND CHILLS AS GLOBAL DEMAND KEEPS THE BUYING FRENZY GOING

PROGNOSIS '96



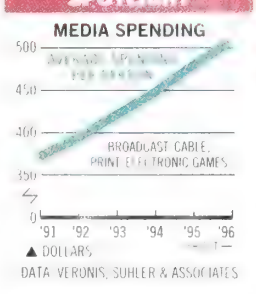
POSITIVES

- The Olympics, the election, and a revived economy should increase TV ad revenue by about 8%.
- Telecom deregulation will spur a burst of investment by phone companies in cable TV.
- Foreign demand for U.S. entertainment remains strong.

NEGATIVES

- Technology disappointments will slow adoption of interactive TV.
- Smaller players may be shunted aside.

Spotlight



It has been more than a decade since television host Monty Hall looked behind that curtain for the last time. But in the frenzied media world, every day seems to be a rerun of *Let's Make a Deal*. Walt Disney Co. plunked down $19 billion in stock and cash to buy Capital Cities/ABC Inc. Westinghouse Electric Corp. bought CBS Inc. News Corp. Chairman Rupert Murdoch jumped on the Internet, launched a sports channel to rival ESPN, and then made plans to beam TV signals to Latin America. And in cable? Last year, a staggering $25 billion in deals were struck, as nearly one in five subscribers saw their cable companies change hands.

In 1996, the media dealmaking won't be confined to the TV and movie businesses. *USA Today* publisher Gannett Co. is still on the prowl after completing its $1.7 billion purchase of Multimedia Inc. Other publishing deals may be in the offing. Spurring on the activity is an unquenchable worldwide thirst for American-made movies and TV programs—and a surprising rebound in Americans' appetite for the printed word.

Programming and distribution entities will keep getting married in 1996—programmers to ensure an outlet for their works, distributors to fill their pipelines. General Electric Co. is likely to go shopping for partners again this year, after failing in 1995 to persuade Disney to buy a half-interest in its NBC Inc. unit. Possible candidates: Seagram's MCA subsidiary, which includes Universal Pictures, or Sony's Hollywood-based studios. Microsoft Corp., a partner with NBC in an on-line news channel, could also be a bidder. After buying CBS, Westinghouse is still looking to bolster its programming and could strike an alliance with a Hollywood studio as well. "The idea is to protect yourself from being shut out as the big get bigger," says Merrill Lynch & Co. analyst Jessica Reif.

NET GAINS. Propelling the movement toward bigness in 1996 is the expected passage of the long-awaited federal telecommunications bill. Among other things, the legislation would immediately allow cable and telephone companies to compete in one another's markets and gradually raise ceilings on the number of radio and TV stations a company can own. That should prompt a new wave of acquisitions, says G F. Jankowski, managing director at Vero Suhler & Associates Inc., a New York inv ment bank. Among those rumored ready to is billionaire Ronald O. Perelman, whose I World Entertainment Inc. broadcast and duction company is loaded with debt.

Media companies will benefit in 1996 a robust advertising market that for third year running should out form the overall economy. Boo by the Olympic Games in Atlanta U.S. political campaigns, domestic vertising in all media should grow 7.8%, to $174 billion, predicts Robe Coen, a senior vice-president at ad ag McCann-Erickson Worldwide. The major broadcast networks will be ar the biggest winners, with a proje 12.5% increase, to $13 billion.

NEW SYSTEMS. The ad increase isn't only good news for network televi After losing audiences to cable and dicated programming for years, number of sets tuned into the works will stabilize in 1996 at ro ly 64% of those viewing TV, pre Veronis Suhler. But not every work will survive. Time Warner struggling Warner Bros. net will likely seek a merger startup UPN, a joint ventu United Broadcasting and Vi Inc.'s Paramount Pictures C

Cable television, meanw will seek growth by adding vices rather than subscri After adding 9 million scribers over the previous years, the industry's custo base will grow by roug million in 1996, accordin Veronis Suhler. To mai the cash-flow growth, companies will need to systems to battle the te and many cable compa will introduce modem ser for high-speed data transfe er in 1996. Other companies, such as Tele- munications Inc., will move aggressively seas into markets with greater potential t subscribers.

Foreign companies—which have sat o sidelines since the disastrous foray of Ja ese companies in Hollywood—will also ree on the American media scene. The sale of ner Broadcasting System Inc. to Time Wa

ed many of them to the dwindling number ompanies available to fill the Information erhighway with films and TV shows. Dutch ronics giant Philips' PolyGram entertain- t unit will aggressively seek an acquisition. night German media powerhouse Bertels- n, which recently opened a flashy Los An- s headquarters. One likely target is MGM/UA, h is rising from the ashes with such films as *lenEye* and *Get Shorty*. The studio's owner, ich bank Crédit Lyonnais, recently hired stment bankers Lazard Frères & Co. to off the studio.

R PROFITS. Other bidding wars will feature Corp.'s Los Angeles film unit and Thorn record division. Murdoch is a possible bid- for EMI. So is Disney, which has a small rd company with few stars. The biggest ing war, however, could center on Sony. r parting ways with U.S. CEO Michael P. lhof, Sony is likely to try unloading a piece s film company. Sony insiders say Murdoch expressed interest. Investment bankers say s eager to line up more content for broad- ng. And, despite his frequent denials, Mi- oft Chairman William H. Gates III may be interested.

ollywood production will increase in 1996 to fy the booming foreign market and domes- able operators. The year will feature more the usual numbers of retreaded oldies. ersal Pictures, with fresh capital from new er Seagram, will churn out films based on TV shows *McHale's Navy*, *Flipper*, and *eant Bilko*. Tom Cruise will headline a film ion of *Mission: Impossible* from Viacom's mount Pictures unit.

ie newspaper business lacks Hollywood's but had a marquee year in 1995, with ings gains of 14.8% at 11 big newspaper ishing companies, according to Donaldson, in & Jenrette (DLJ) Securities Corp. McCann-Erickson's Coen says that in 1996, advertising revenue will increase by a modest 5.5%, to $4.25 billion, down from an 11% rise through the first nine months of 1995. That will dampen industry earnings growth to an average of 6.5% in 1996, DLJ says.

Those kinds of returns don't satisfy many newspaper publishers, who say they need to make drastic cost reductions to ensure their long-term health. "We're starting to see a little breathing room, but not an awful lot," says Mark H. Willes, Times Mirror Co.'s new CEO. In 1995, Willes cut hundreds of jobs at the flagship *Los Angeles Times* and closed the New York City edition of Long Island-based *Newsday*.

Still, newspaper companies are hardly turning their backs on their printing presses—high paper prices and the Info Highway notwithstanding. Evidence of that is Gannett's purchase of Multimedia. Also, in 1996, *The New York Times* will launch a Northeastern edition, while the *Los Angeles Times* will revive plans to distribute its paper in Washington, D.C.

Why the newfound optimism? For one thing, readership of newspapers is up as the number of Americans 35 and over expands. Those demographics will also help book and magazine publishers. In 1996, a slew of new specialty magazines will likely hit the newsstands. Century 21 Real Estate Corp., for instance, will launch a new home magazine with Hachette Filipacchi Magazines Inc. Book publishers intend to expand their lines to fill the shelves of book superstores and discount chains. Hearst Corp. will soon launch its first hardcover line for adults. Even MTV will have its own book line, geared to the under-35 crowd.

Which media companies will strike the audience's fancy in 1996? That's hard to say. But these days, if you can't produce a hit you can always buy the hitmaker.

By Ronald Grover in Los Angeles

■ Coming attractions may include a juicy bidding war over Sony's Hollywood studios. Could Jack Welch and Rupert Murdoch play starring roles?

THE BABY BELLS TAKE THEIR FIRST STEPS IN TINSELTOWN

s he stood before his shareholders at Ameritech Corp.'s annual meeting, chatting via a video ookup with Mickey Mouse, Chief xecutive Richard C. Notebaert ft little doubt that the telephone mpanies' pin-striped world had efinitely gone Hollywood. In 1996, a wide swath of head-to-head nfrontations from San Diego to hicago, the Baby Bells intend nally to launch their attack on the ble-television industry.

The sweeping telecommunications ill in Congress would allow phone mpanies to challenge cable opera- rs outside their home markets im- ediately, and within their regions nce they prove their phone busi- ess faces competition. At first, hone-company offerings won't look all that different from what TV viewers get now by handing over $40 to $50 each month to their local cable companies. Down the road, however, the phone companies hope to beat the cable companies to the interactive market with such features as home shopping and games. "The idea is to outdo the cable companies, not just match them," says Howard Stringer, chairman of the Tele-TV venture that includes three of the seven Baby Bells.

First off, the telcos plan to offer more channels. In Glendale Heights, Ill., Ameritech's network of optical fiber and copper cable will offer 90 channels, compared with the local cable operator's current 60. In Riverside, Calif., where the 90 channels will be delivered over the air through a system called wireless cable, the reception is expected to be sharper. With only 15% of Riverside County receiving cable, Pacific Telesis Group expects to make inroads by stuffing marketing literature into the weekly phone bills it sends in the area.

The telcos won't lack programming firepower, either. Walt Disney Co., a partner with three of the Baby Bells and GTE Corp. in another joint venture, has assigned top animators to work on tailor-made programming, including a souped-up on-screen guide. As for Tele-TV, Stringer says it has a production facility ready for action. For phone companies, Hollywood will be quite a change from selling call-waiting service.

By Ronald Grover in Los Angeles

THE PATIENT IS STABLE—FOR NOW

HEALTH-CARE COSTS ARE IN CHECK, BUT THE INDUSTRY'S UPHEAVAL ISN'T OVER

PROGNOSIS '96

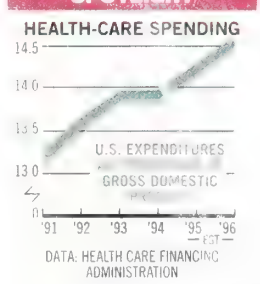
POSITIVES

- For-profit hospitals should continue to gain market share and see admissions rise modestly.
- Well-managed nursing homes will pick up business as hospital stays continue to shrink.

NEGATIVES

- Rising cost pressure from managed care, plus lower Medicare and Medicaid rates, will keep a squeeze on margins.
- Health-care reform hasn't addressed the uninsured, who will put an even greater strain on the system.

SPOTLIGHT



A deceptive peace has descended on the nation's $750 billion health-care industry. There has been no word of a major health-maintenance organization merger for months. Hospital giant Columbia/HCA appears too occupied digesting the acquisitions of years past to indulge its unrelenting appetite. And once again, reform sits deadlocked on Capitol Hill.

But just wait: Beneath the surface, a revolution rages on. "The pace of change is stunning," says Dr. W. Allen Schaffer, head of managed care at CIGNA Healthcare Inc. "We have to reevaluate our strategic assumptions every six months." Managed-care plans snatched some 5 million Americans from their traditional health insurers in 1995, bringing total enrollment in HMOs to 56 million. Those are powerful numbers, and managed care now calls the shots. This year, it likely will force more consolidation than ever.

The industry, still fragmented and unwieldy, remains eminently ripe for restructuring. Even though health-care inflation has slowed, spending continues to edge upward as a share of the nation's economy (chart). Massive overhead associated with excess capacity remains, and "the only way to slow growth in health-care spending is to debloat the system," says John F. Hindelong, an analyst at Donaldson, Lufkin & Jenrette Securities Corp.

That process is under way. Indeed, employers saw their health-care costs drop in 1994 and remain flat in 1995 as millions of workers moved into cheaper managed-care plans. Employers' costs will probably rise slightly on average in 1996 as fewer additional employees switch to managed care, according to Foster & Higgins consultant John Erb.

TEAMING UP. The cost squeeze means more upheaval for doctors and hospitals. "The market works, but it is very painful," says Robert L. Montgomery, chief executive at Alta Bates Health System in Berkeley, Calif. Alta Bates, forced to hold managed-care charges flat for a third straight year, has joined a hospital consortium to amass a total of 600,000 managed-care patients—the better to negotiate with ever-larger HMOs. Even big, for-profit chains are looking at admissions increases of only 1% to 3% in 1996, says DLJ's Hindelong, though consolidation will help the sector lift earnings by 15% to 20% next year.

The motivation is irresistible: As of Dec. 1995, the industry had seen a record 433 me ers and acquisitions, according to Securit Data Co. Increasingly, those mergers are cr ing industry boundaries—producing new "i grated delivery systems" that put hospit doctors, nursing homes, and others under same corporate roof. The object: one-stop sh ping for managed-care companies, who requ access to a broad array of services, says Co ers & Lybrand consultant Glenn A. Shively

CRAWLING REFORM. At the same time, H are themselves driving for size, market pe tration, and efficiency. Growth certainly w come from rate hikes: Even the better HMOs win premium increases of just 1% to 2% year, says analyst Kenneth Abramowitz of S ford C. Bernstein & Co. Rather, the HMOs n new bodies. Many will see big reve gains this year as more Medicare recipie move into managed-care plans—a s that would accelerate if health-care form succeeds.

And what of reform? Repu cans and Democrats alike w to cut back on payments Medicare service provid And doctors and hospitals an enormous hit from a p posed provision requiring payn reductions if total Medicare spe ing exceeds budget. The outlook Medicaid is particularly cloudy— reason many insurers are sta away from the business.

In any case, governme change will prove, as always less powerful than the mar driven charge for critical n and market muscle. The resul shakeout will be dramatic. In try executives suspect that Aetna & Casualty and CIGNA, both on verge of shedding hunks of their prope and-casualty businesses, could spend h sums to turn their middling health busine into national HMOs.

Such new players, if well-conceived and quately funded, could transform a compartm talized industry that until now has fough battles largely within cities or regions. "By end of the decade, we will begin to see endgame appear," says Gennaro J. Vasil longtime hospital executive who recently came head of Gemini Consulting Inc.'s N American health-care practice. And some hints should come even sooner.

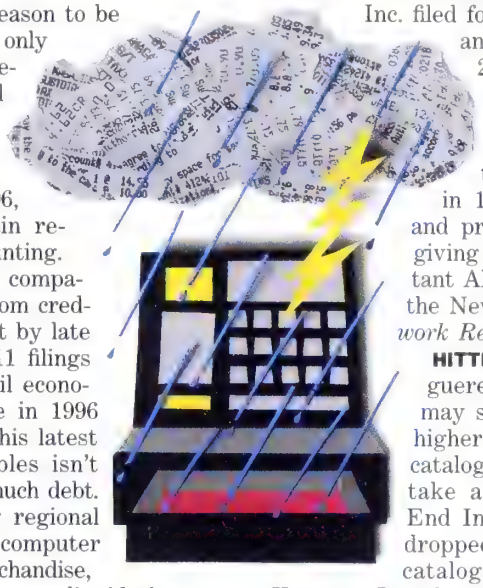
By Keith H. Hammonds in New

GLOOMY DAYS ARE HERE AGAIN

EPARTMENT STORES SHOW PROMISE, BUT SLUGGISH SALES COULD SINK MANY MERCHANTS

onsumer confidence is up, and the stock market is at record highs. But instead of preparing for a stampede to the malls, hants expect a Darwinian shakeout in 1996. strong are getting stronger. The weak lisappearing or consolidating," says Arthur Iartinez, chairman and chief executive of s, Roebuck & Co.

any retailers have reason to be ny. Retail sales rose only during 1995, far be- the 7% annual th common during roaring 1980s. 're expected to rise ie same 4.5% in 1996, e profits will remain re- ned by heavy discounting. ughly 15,000 retail compa- sought protection from cred- in bankruptcy court by late pushing Chapter 11 filings)% from 1994. Retail econo- expect even more in 1996 t). That's because this latest d of financial troubles isn't rom taking on too much debt. oncentrated among regional lers with outdated computer ms, yesterday's merchandise, aging stores. For many, liquidation may ie only answer, says Carl E. Steidtmann, economist of Management Horizons, a ilting unit of Price Waterhouse based in mbus, Ohio.



e trouble is, consumers just aren't spend- uch. Incomes are fairly stagnant, and con- rs' non-mortgage debt-to-income ratio hit l-time high of 19% in late 1995. What's , baby boomers are paying more for ser- , from child- to elder-care, leaving them or shopping. And consumers have discov- that they can get hefty discounts by wait- or sales. "Now that we've taught them to iat, we shouldn't sit around and wonder ' says John Ronzetti, vice-president of the nal Retail Federation.

IT'S CONTRACTION. Discounters are feel- lot of pain. A raft of regional chains, in- ig Bradlees Inc. and Caldor Corp., sought ter 11 protection in 1995 as competition fast-growing Wal-Mart Stores Inc. and et Stores intensified. The shakeout may claim Kmart Corp., the nation's third- st retailer, retail experts say. Kmart CEO l Hall, who replaced the ousted Joseph E. nini in June, says he will close 70 stores in cut $300 million in costs, and continue to unload inventory. "The best answer to Chapter 11 [talk] is to have a solid performance under our belt," he says.

Easier said than done. Just ask specialty retailers, who are expecting another drab year for apparel sales. Clothing sales are expected to grow only 3.5% in 1996 after a 2.5% increase in 1995. St. Louis-based Edison Brothers Stores Inc. filed for Chapter 11 in November and plans to close 500 of its 2,700 mall-based shops. Ann Taylor Stores Corp. is heading for a makeover after suffering a double-digit tumble in same-store sales in 1995—the result of fashion and pricing miscues in an unforgiving market, says retail consultant Alan Millstein, who publishes the New York-based *Fashion Network Report*.

HITTING THE GAS. For beleaguered catalog companies, 1996 may spell a bit of relief. Hit by higher paper and postage costs, catalogers saw their bottom lines take a beating in 1995; Lands' End Inc. profits through October dropped 61%. A survey of U.S. catalogers by consultant A.T. Kearney Inc. found 62% expect sales to increase in 1996.

Department stores should continue to slowly regain market share from outlet stores and off-price retailers. Lower prices—and thinner margins—are the key. "We've had to get our costs down to offer fashion that's also a value," says Allan Questrom, CEO of Cincinnati-based Federated Department Stores Inc., parent of Macy's and Bloomingdale's.

Consumer-electronics stores are expected to have another hot year, as shoppers snap up computers and related items. That means strong revenue growth for category killers—high-volume specialty chains such as Best Buy Co. and Circuit City Stores Inc. But they, too, must settle for the slimmest of margins.

Sears seems to be getting the formula right. It's one of the last department stores with a broad array of hard goods, such as appliances and computers. With these products going gangbusters and its apparel share expanding, Sears is winning market share. Says CEO Martinez: "When that happens, you push the accelerator a little harder." But in what looks like a treacherous 1996, many other retailers will be satisfied just to stay on the road.

By Susan Chandler in Chicago

PROGNOSIS '96

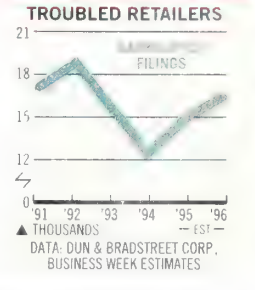
POSITIVES

- Housing purchases should continue to help sales of home-related goods.
- Consumer confidence is rising, and that bodes well for sales of big-ticket items such as home computers.

NEGATIVES

- Apparel sales will continue to be slow as consumers focus on home-related purchases.
- Retail bankruptcies will increase as the shakeout among discounters and off-price retailers continues.

SPOTLIGHT



PICKING UP SPEED

AIRLINES ARE FINALLY IN THE CLEAR—AND RAILROADS MAY LINK UP

PROGNOSIS '96

TRANSPORTATION SERVICES

POSITIVES

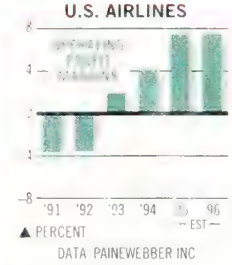
- Airline capacity should grow more slowly than traffic, meaning fuller planes and higher fares.
- Railroads are boosting productivity with computerization and faster locomotives.

NEGATIVES

- Airlines will be hard-pressed to win cost reductions from labor when profits are soaring.
- The trucking industry is suffering from excess capacity.
- Railroads have yet to sign contracts with about a dozen unions.

SPOTLIGHT

U.S. AIRLINES

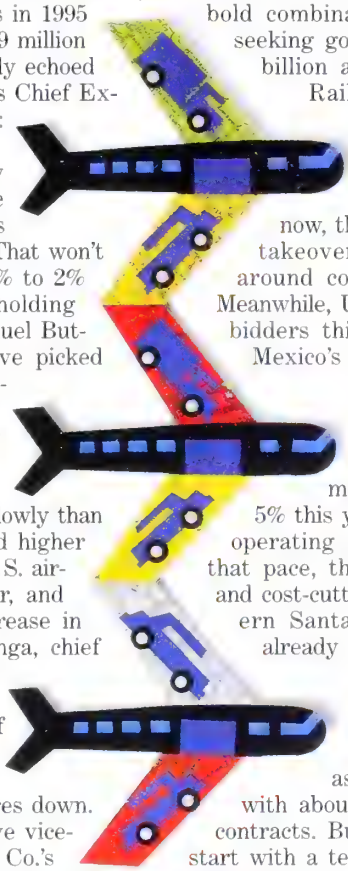


Transportation services expect modest growth in 1996, with airlines and railroads faring best and truckers bringing up the rear. All three sectors are focusing on improving productivity—and keeping a close eye on the merger scene.

Airline executives are happiest: After five years of losses and retrenchment, the industry has finally recovered. Net profits in 1995 totaled about $2 billion, vs. a $279 million loss in 1994. In a sentiment widely echoed by his peers, Continental Airlines Chief Executive Gordon M. Bethune says: "It's a pretty rosy-looking '96."

With traffic expected to grow only about 3% in 1996, airline profits will hinge on keeping costs in check and capacity usage up. That won't be easy. Unit costs will rise 1.5% to 2% for the major carriers, after holding steady in 1995, says analyst Samuel Buttrick of PaineWebber Inc. "We've picked the low-hanging fruit," agrees Delta Air Lines Inc. CEO Ronald W. Allen. "It's going to get tougher from here on out."

The good news for airlines is that capacity should grow more slowly than traffic, meaning fuller planes and higher fares. Systemwide capacity for U.S. airlines grew about 2.5% last year, and it's likely to show a similar increase in '96, estimates David A. Swierenga, chief economist for the Air Transport Assn. That bodes well for fares. True, the rapid expansion of such low-cost carriers as Southwest Airlines Co. and ValuJet Airlines Inc. will help to hold fares down. But Edward P. Gilligan, executive vice-president for American Express Co.'s Travel Management Services, predicts that airfares will rise an average of 3% to 4% this year, with only limited and carefully targeted discounting.



BOLD COMBINATIONS. The airlines' discipline is expected to translate into higher profits. A bullish Steve Lewins of Gruntal & Co. figures major airlines' earnings will soar 56% from 1995's modest level. The rising profits complicate carriers' efforts to wrest major concessions from their pilots so they can better compete with lower-cost carriers. Still, pilots at American and Delta have recently announced a willingness to consider wage and work-rule changes on short-haul routes that airlines have been farming out to other carriers.

There's still one unsettling question as the industry reaches cruising altitude: Will airline mergers mar the flight plan? A new rou[nd] dealmaking could distract execs from rebu[ilding] balance sheets and improving service. U[nited] Airlines Inc. decided last year not to pur[sue] marriage with USAir Inc. And American s[ays] won't strike first. Still, no one rules out a[nother] wave of merger mania in 1996.

Railroads, in contrast, are already pur[suing] bold combinations. Union Pacific Co[rp.] seeking government approval for its $[4] billion acquisition of Southern P[acific] Rail Corp. Its deal comes i[n] sponse to Burlington N[orth]ern Inc.'s $4 billion pur[chase] last year of Santa Fe P[acific] Corp., creating, at leas[t] now, the nation's largest railroad. A takeover rumors continue to [swirl] around companies such as Conrail. Meanwhile, U.S. railroads are expected [to] bidders this year in the privatizati[on] Mexico's railroads.

Even without such deals [in]vestors have much to c[heer] about. Merrill Lynch & Co. [ana]lyst Michael H. Lloyd ex[pects] modest revenue gains of 4[%] 5% this year for the major railroads. operating profits should grow at d[ou]ble that pace, thanks to productivity incre[ases] and cost-cutting. The new Burlington N[orth]ern Santa Fe Corp., for example, already slashed jobs and has also id[enti]fied almost $1 billion in [annu]ating cost savings over [the] next few years.

Labor remains a wild [card] as the railroad industry bar[gains] with about a dozen unions to reach contracts. But bargaining is off to a st[rong] start with a tentative accord with the U[nited] Transportation Union, representing 25[,000] workers.

Truckers are hoping simply to bounce from a bleak 1995. The industry has been [ham]mered by a slowing of U.S. economic grow[th], downturn in exports to Mexico, and exces[sive] pacity. After a banner 1994, bullish truc[king] companies rapidly expanded their fleets [with] bigger trucks. Now, with softer demand [and] lackluster earnings, analysts expect a sh[ake]out. Swift Transportation Co., for one, is h[ard] to benefit: The company has made four acq[uisi]tions since 1991 and is prowling for m[ore]. Truckers will have to satisfy themselves [with] such hardscrabbling while railroads and air[lines] enjoy a relatively smooth ride.

By Wendy Zellner in D[allas]

LL TOGETHER NOW: 'MAKE THAT TO GO'

SATIABLE DEMAND FOR CONVENIENT, READY-TO-EAT MEALS HAS THE FOOD BIZ SCRAMBLING

ston Chicken Inc. didn't expect much when it tested ready-made holiday meals his past Thanksgiving. But customers ed in, gobbling down hundreds of roast ys with all the fixin's. Why? "People don't have time to cook Thanksgiving turkey r," says Saad J. Nadhir, co-chairman of ake-out chain.

1996, the nation's $900 billion food industry e at the mercy of customers who don't time. Shoppers who can barely steal a noments to shop—let alone whip up home-d feasts—will set the pace of growth for processors, retailers, and food-service s. The edge will go to big, dominant com-s that can use marketing clout to expand e of stomach" at the expense of weaker etitors. Other winners will be innovators of es that find new ways to ease the hunger s of a harried populace.

evitably, the time squeeze on shoppers will e losers, too, especially among traditional ie supermarkets. Their strong flows give them enviable ig power, so an imme- shakeout is unlikely. rosion will continue ermarkets face off st up-and-comers as Nadhir, who es- es that half the customers at st-growing Boston Chicken would otherwise have d at home. "You have iany retailers compet- ir too few food dollars ppealing to consumers iave less time to deal it," says consultant Z. Stern of Chicago's llan & Doolittle.

OVENS. Food processors restaurant chains will see o 6% revenue growth in Stern estimates. Supermarkets ke out 2% to 3% growth, barely even with ion. As U.S. households prepare fewer at home, the percentage of food dollars at food retail stores—as opposed to irants, cafeterias, convenience stores, and ke—will dip to 48% in '96 from 55% a e ago (chart). "It's a great threat to su-arkets," warns John H. Bryan, chief exec- officer for Sara Lee Corp.

nsumers clamoring for ready-to-eat meals made deli sales the one supermarket t spot. Supermarket chains such as Byer- Edina, Minn., and Dominick's Finer Foods in Northlake, Ill., have pioneered new in-store formats. In '96, expanded deli departments will attract at least 8¢ of each food dollar, up from 4¢ in 1986. And watch for more supermarkets to introduce mall-style food courts featuring proven operators such as McDonald's Corp., which is testing outlets at a Farmer Jacks supermarket in Michigan and a Kroger in Tennessee. Food processors will join in, too: Sara Lee has 17 sandwich shops serving its premium deli meats inside Kroger supermarkets in Texas and Ohio.

Among restaurant chains, cost control will be crucial. McDonald's has cut the cost of opening a new restaurant by 30% over the past five years through standardization and more reliance on drive-thru layouts. That has helped McDonald's step up its U.S. growth fivefold, including joint ventures that have put Golden Arches in Wal-Mart Stores, Home Depots, Incredible Universe home-electronics stores, and Amoco gas stations.

FAR AND AWAY. With so many more outlets at hand, busy shoppers visit more often, leaving less on the plate for the competition. Says McDonald's Vice-Chairman Jack M. Greenberg: "If you can dominate a trading area, it's much more difficult and expensive for competitors to take customers away from you."

Dominance matters to food processors, too. They're struggling to increase scale and efficiency to satisfy the likes of supercenters, which combine cut-rate supermarkets and discount stores under one roof. Food processors also hope to give their ho-hum U.S. results a boost by pursuing fast-growth markets overseas. And sharp operators such as H.J. Heinz, CPC International, Campbell Soup, and others will be trying to lock in relationships with fast-growing food-service operators. "Everybody has the same three strategies—lower domestic costs, grow internationally, and push into food service," says analyst John M. McMillin at Prudential Securities Inc.

With all hands reaching for the same brass ring, the strongest brands rule. As in 1995, industry players will sell off weak units to more dominant competitors and buy businesses that enhance existing strengths. The goal? Be No. 1. "I'm not even sure being No. 2 is enough anymore," McMillin says. For investors, the message is clear: In the scrap over "share of stomach," bet on the top dogs.

By Greg Burns in Chicago

PROGNOSIS '96

FOOD MANUFACTURING, RESTAURANTS, & FOOD STORES

POSITIVES

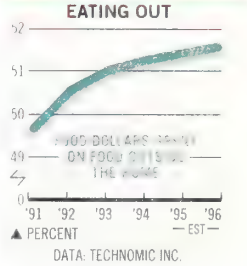
- With more consumers eating on the run, companies emphasizing convenience will find eager customers.
- Food-service operators will grow by opening outlets in stores, supermarkets, and gas stations.

NEGATIVES

- Value-conscious shoppers will resist price increases.
- Supermarkets will continue to lose "share of stomach" to sharper food-service operators, such as Boston Chicken.

SPOTLIGHT

EATING OUT



MIGHTY MORPHIN POWER REARRANGERS

DEREGULATION WILL TRANSFORM THE INDUSTRY—AND CONTINUE TO PINCH PROFITS

PROGNOSIS '96

UTILITIES

POSITIVES

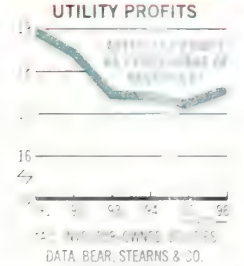
- Low interest rates have lightened debt loads.
- Delay in deregulation is allowing utilities more time to prepare.
- Demand for power is rising, and capacity is ample, so there's no need for costly construction.

NEGATIVES

- Demands by big customers for lower prices are hurting margins.
- High-cost utilities face a bleak future in a deregulated world.

SPOTLIGHT

UTILITY PROFITS



"Exciting, intense, and fun": That's how a prominent electric-utility executive describes his job these days. Surprised? If you thought electricity was about as thrilling as dentistry, look again. A three-year-old drive toward deregulation is causing new upheavals, from cut-rate pricing to an unprecedented surge in mergers.

On the regulatory front, the action in 1996 is likely to get a jump start from an innovative plan approved by California's Public Utilities Commission at the end of 1995. The plan, subject to change, would let some customers shop for electricity from rival suppliers starting in 1998. The long-awaited decision is another sign that the economic and political forces propelling deregulation are too powerful to halt. Even American Electric Power Co., the nation's second-largest investor-owned utility—and at one time a staunch opponent of competition—proposed its own far-reaching deregulation plan in 1995. Rather than fight the tide, says Charles A. Falcone, an AEP senior vice-president, "we have decided we want to help shape the industry's new structure."

SMOOTH SHIFT. AEP and other utilities had little choice. Profits will be boosted or ravaged for years depending on how the industry and regulators resolve some vexing questions. One big one is how far competition should go. The most radical approach would let customers choose an electricity supplier just as they choose a long-distance phone carrier, with power flowing over still regulated lines maintained by the local utility. A more moderate approach would retain today's basic structure but require utilities to set rates based on prices in a wholesale power pool, which proponents say would cut down on confusion. Muddying the waters, California regulators decided to let both approaches coexist.

Then there's the issue of the billions of dollars in uneconomical power plants and long-term power contracts on the books of many utilities. These will become millstones in a world where the cheapest power suppliers will prevail. Big customers and some low-cost utilities contend that overly expensive power plants and contracts should be written off, forcing shareholders to bear the brunt of utilities' past poor decisions. But most utilities argue that their costs are largely a legacy of poor regulations, so customers should continue to foot the bill for a period. Allowing customers to disregard their obligations "is like asking your bank to let you walk away from half your mortgage just because you want a new house," argues Thomas May, CEO of Boston Edison Co.

READY TO BID. More states will grapple with these and other contentious issues in 1996, starting with Massachusetts and New Hampshire. Meanwhile, utilities are shedding costs and their monopolistic mind-sets. Boston Edison dumped one-fifth of its managers in 1995 and tried to spur new thinking by reassigning most of those remaining to new jobs. WPL Holdings Inc.'s low-cost Wisconsin utility, for example, offered to show rivals' customers how much they could save by switching to WPL. It can't wrest away many customers now, but it hopes to have the chance soon. "Nobody owns customers," says Erroll B. Davis Jr., WPL's aggressive CEO.

Despite cost-cutting, profit margins aren't likely to improve much after a five-year slide. Why? To stop defections, many utilities are cutting prices to big customers 10% to 40% in return for long-term commitments. Average after-tax profit margins declined to 17.2% in 1995, from 18.9% in 1991, says Daniel Scotto, an analyst with Bear, Stearns & Co.

Moreover, some high-cost utilities are carrying artificial assets on their books, such as payments due from customers over the next 20 to 30 years. If deregulation proceeds far enough, utilities may have to switch to industrial accounting standards that don't recognize such assets. The resulting megawrite-offs "could be very ugly," says analyst Scotto, who cites Centerior Energy Corp. as a prime candidate. Some utilities could be forced into a restructuring or even bankruptcy.

Also on tap for 1996 are more dividend hikes by an industry where dividends once provided almost the only investment appeal. And many others, which reached a record $11.9 billion in 1995, are likely to keep surging, especially if stock prices start to plummet as competition takes hold. No question about it: The electric utility industry isn't boring anymore.

By Mark Maremont in Bo

WHO SAYS YOU CAN'T FIND GOOD HELP?

BUSINESS-SERVICE FIRMS BOOM AS COMPANIES AROUND THE GLOBE RETOOL

n some recent continent-hopping business rips, George T. Shaheen, managing partner for Andersen Consulting, became thorly convinced that change knows no bound. The rage in China was all about restruc- and developing new markets. A Brazilian mpany was worried about how to com- in foreign countries. "It doesn't matter e you're doing business," says Shaheen, yone is going through a massive retooling." e that may be wrenching to many, for An- n and other providers of business services, aval is a boon.

siness services—a new category in BUSIWEEK's Industry Outlook—encompasses leervices, advertising, personnel supply, reh and consulting, accounting, engineering, tecture, and miscellaneous others, such as ment rental and leasing. While their growth vary, all of these industries to some degree in on the continuing global trend toward ng outside help. In 1996, predicts DRI/Mc-Hill, business services will grow 3.5% after on, to $806 billion in 1995 dollars.

nsultants such as $4 billion Andersen d do far better than that. Andersen, which alizes in providing advice on systems and led change management, expects business e 20% for a second year and to add as as 8,000 people to its workforce of 37,000. time, Bain & Co. figures its business will 30% this year on the back of its "growth"

lting, which advises once shrinking clients o grab market share and find new cus- s overseas.

FEVER. Business-service providers will on jobs of increasing sophistication. Cor- e layoffs will remain in the range of last 420,000 or so, figures outplacement firm enger, Gray & Christmas, so companies ontinue to off-load everything from public ons to computer services. That will en- a fourth year of strong growth for the orary-help sector, which the National Asion of Temporary & Staffing Services estimates has annual revenues of $40 billion (chart). "Temporary help used to be for emergency needs," says Manpower International Inc. Chairman Mitchell S. Fromstein. "Now, it's part of a company's ongoing workforce strategy." Fromstein expects Manpower revenues to be up some 15%—even higher than the industry's healthy 9% rise.

At Manpower, as at scores of other companies, growth is being fueled by demands for special skills. Today, Manpower is supplying computer programmers and systems integrators as well as clerical workers. Industrial-design specialists such as Boston's Design Continuum Inc. are working with clients from research to final production. In advertising, efforts to commercialize the Internet are providing golden opportunities for nimble upstarts. "The Internet will pose a major challenge for the big agencies," says analyst James D. Dougherty of Dean Witter Reynolds Inc.

WORK, WORK. Generally, though, size seems to be an advantage. As industries consolidate, companies turn to providers that can handle business globally. In the advertising business, where growth is expected to be nearly 8% thanks to election and Olympics spending, "it's increasingly difficult for midsize [advertising] agencies to compete," says Rochelle Lazarus, CEO of giant Ogilvy & Mather Worldwide Inc.

So look for the fragmented business-services sector to spawn plenty of mergers. Last year, EDS Corp. purchased A.T. Kearney for $600 million, marrying computer systems and engineering knowhow. This year, law firms are ripe for combination, says consultant Bradford W. Hildebrandt. While law firms are recovering from the depressed early '90s, Hildebrandt expects revenues to rise 10% in 1996, so regional, national, and even international mergers should be on the uptick. "We'll see global consolidation like we began seeing in accounting 10 years ago," predicts Hildebrandt.

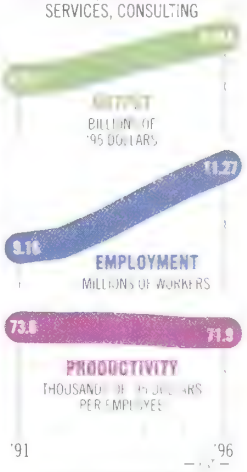
Other forces driving the mergers: difficulty in finding top professionals and pricing pressure from customers. More and more companies are demanding fixed fees from law firms. The outplacement industry has seen commissions on large contracts drop from as much as 17% per individual to about 10%, according to John A. Challenger. Yet across most of the growing services sector, "the No. 1 risk and temptation" is to take on more work than firms have the ability to handle, say Bain's worldwide managing director, Thomas J. Tierney. For now, that's a hurdle most service providers are eager to attempt.

By Richard A. Melcher in Chicago

PROGNOSIS '96

BUSINESS SERVICES

INCLUDES LEGAL SERVICES, ADVERTISING, PERSONNEL SUPPLY SERVICES, CONSULTING



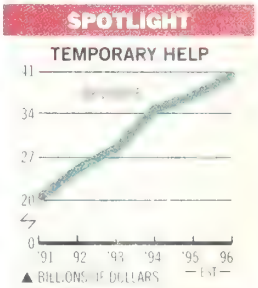
POSITIVES

- Continued industry restructuring favors a variety of services, from temporary help to consulting and engineering.
- Booming economies in Asia and other markets offer new work to U.S. architects, engineers, and advertisers.

NEGATIVES

- A shortage of quality staff looms as businesses demand more sophisticated services.
- Consolidation among clients adds price pressures and kills smaller or less specialized firms.

SPOTLIGHT



DATA: NATSS, MANPOWER INC. ESTIMATES

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FINANCE

BANKING
A few blots on the ledger—including heavy consumer-loan burdens and dubious corporate-debt quality—should temper an otherwise bully year
PAGE 110

SECURITIES
The good times will keep rolling on Wall Street: Interest rates are staying in the cellar and the M&A locomotive shows no sign of slowing down
PAGE 111

REAL ESTATE/ CONSTRUCTION
Continued strength in the housing market and high-rise expectations in the office sector should help bolster the slow performance in retail construction
PAGE 112

INSURANCE
Core weaknesses in property-casualty and life insurance, along with "too many players competing for too little return," mean the watchword for '96 will be consolidation
PAGE 114

ILLUSTRATIONS BY BRIAN CAIRNS

A FEW NEW BLOTS ON THE LEDGER

DELINQUENT CONSUMER LOANS AND SKINNY MARGINS MAY TEMPER AN OTHERWISE BULLY YE

PROGNOSIS '96

BANKING

DATA: DRI/M GRAW HILL

POSITIVES

- The financial condition of banks is excellent and leaves them well prepared to weather any economic slowdown.
- Managed properly, the ongoing consolidation in the industry will make it more efficient.

NEGATIVES

- Consumers have been loading up on debt, and consumer loan delinquencies are rising.
- Profit margins on consumer and corporate loans could decline, hurting bank earnings.

SPOTLIGHT

BIG BANKS

DATA: MERRILL LYNCH & CO

It was beginning to look as if the good times would never end for U.S. banks. Since 1991, profits have set record after record, asset quality has sharply improved, and bank stocks have seemed headed for the moon. But now, a few clouds are dotting the horizon. Consumers are beginning to have trouble with heavy debt burdens. And the narrow gap between short- and long-term rates bodes ill for banks' profit margins on loans and investments. Although Merrill Lynch & Co. predicts that profits for 56 top banks should grow 9.8% in 1996 (chart), pan in for a closeup and the picture is murkier.

The biggest potential problem is related to the ongoing growth in lending. Consumer installment credit grew roughly 14% in 1995, according to DRI/McGraw-Hill. While banks profit initially by providing that credit, heavy consumer debt burdens mean more loan delinquencies down the road. Indeed, the American Bankers Assn. says that late payments on bank-card accounts have risen for four quarters in a row and are currently at their second-highest level in 10 years. "Consumer credit quality is, I think, a very big short-term issue, potentially a big minefield," says Judah Kraushaar, a banking analyst at Merrill Lynch.

HARD TO FUDGE. Corporate lending is also expanding rapidly, raising additional concerns about loan quality in 1996. James B. Lee, vice-chairman at Chemical Banking Corp., the top bank in loan syndications, says corporate lending will increase through 1996, but "certain [industry] sectors will continue to deteriorate." That will prompt some borrowers to fall behind on payments or default. Lee says lending standards are far higher than they were in the late 1980s. However, the intense competition to make many loans suggests that some banks are willing to offer loan terms that leave little room for error.

Then there is the problem of profit margins. Today, there's less than one percentage point between the short-term rates at which banks borrow and the longer-term rates at which they typically lend. That means room for profits is scarce. A 1995 study by Merrill Lynch shows that bank stocks have been poor performers nearly every year following periods when short- and long-term interest rates are close together. "This is a hard yield curve to work with," says Jeffrey C. Keil, president of Republic New Corp.

Luckily, banks still have plenty of win their backs. While loan delinquencies are ri they are still relatively scarce, and banks ne use only small portions of their earnings a serves for bad credits. Moreover, new busine are expanding for some of the biggest b At J.P. Morgan & Co., Thomas B. Ketch head of investment banking for the Americas pects corporate-finance fees for services su advising on mergers to increase 40% in 19

Expect many banks to be intensely cost scious in the coming Bank mergers will likely tinue at gale force: Ge Smith, managing direct the financial institut group of UBS Securities predicts that by 2000, th 50 banks will control 80 the assets in the U.S. b ing industry, up from 56 day. And many deals wi predicated on massive savings.

REFORM DELAY. Spendin technology will grow in Most bankers, eager t their customers reduce use of high-cost branches step up use of electronic banking outlets placing large bets on systems for bankin phone or personal computer. Edward E. Cr field Jr., chairman and CEO of First Union and one of the country's most acquisitive b ers, plans to stop buying banks for five y while he invests in electronic retail ban "As soon as we really do have a choice fo customer to make that's realistic, then he move away from branches," he says.

Changes will be harder to come by on regulatory front. Banks have been stymie the big revisions they sought in 1995, such a end to the barriers between commercial investment banking, and they could we frustrated again. Banks and insurance ag need to agree on provisions to limit the f of banks into the insurance business before banking law reform can move forward.

Having waited this long for deregula bank executives aren't holding their br However, for those who keep a sharp eye o erations, pay close attention to the creditwo ness of borrowers, and plan for electronic b ing, 1996 could be a very good year indee

By Kelley Holland in New York, with Barrett in Washington

WILL WALL STREET HIT A WALL?

IT WILL BE TOUGH TO MATCH '95, BUT LOW RATES COULD KEEP THE MARKET ROBUST

all Street should get another gift from the Federal Reserve in 1996: continued low interest rates. DRI/McGraw-Hill pre- that 30-year Treasury bonds will end the at 6.26%, up just a tad from 6% at yearend Rock-bottom rates mean another super for the securities industry, since investors eep deserting bank certificates of deposits ek higher returns in the stock market, ing the market and Wall Street commis- "From everything we see, it's going to be er good year," declares John J. Mack, pres- of Morgan Stanley & Co.

ter a slow start, 1995 omed into a very good for the securities indus- New York Stock Ex- ge firms reaped an esti- l $6.5 billion in pretax s. That's the second-best ever after 1993's $8.6 bil- low-out. Fueling the in- y was record stock-mar- volume, thanks to a dard & Poor's 500-stock that soared 37% and g underwriting and mu- und sales.

r 1996, the BUSINESS profit estimate is just billion, though. That's because it would be for rates to decline in 1996 as much as did in 1995, when they fell from 8% to 6%. Declining rates are Wall Street's n environment, since they boost corporate ncing as well as the stock market.

OVER RUMORS. The new year is starting ith lots of momentum. Mergers and ac- ions were red-hot in 1995, racking up $450 in deals, topping the previous record of billion in 1994, according to Securities Data There is no reason to believe the robust market won't continue," says Kim Fen- sque, a managing director at UBS Securi- nc. Initial public offerings were another r, with an estimated $29 billion in new in 1995, almost reaching the 1993 record billion.

ll Street is notoriously cyclical, though, e gold rush could slow in '96. The stock et is unlikely to sustain its record perfor- e for two years in a row. The securities in- y also faces excess capacity: Too many are fighting for the same business. Ag- ive up-and-comers range from Germany's che Bank and Union Bank of Switzerland S. commercial banks. "It's a difficult chal- to continue to maintain high margins," says Jerome P. Kenney, a Merrill Lynch executive vice-president.

With so much competition, consolidation is expected to continue in 1996. Rumors constantly have firms dressing themselves up for sale. Some of them, such as Lehman Brothers Inc., PaineWebber Inc., and Prudential Securities, are medium-size firms that are finding it expensive to compete internationally. Meanwhile, Goldman Sachs, Merrill Lynch, and Morgan Stanley are spending heavily to position themselves as global competitors that can remain independent. "In 1996, the large will get larger, small boutiques will prosper, and those in the middle will get squeezed," says Bruce S. Foerster, president of South Beach Capital Markets Advisory Corp. in Miami.

Whether large or small, brokerage stocks are due for a correction. Analysts aren't as hot on them, since they had a spectacular rise in 1995. Merrill Lynch & Co. shares rose 51% through mid-December, and Charles Schwab & Co. was up 86%. Mergers and acquisitions, hottest in banking and media, might lose some steam.

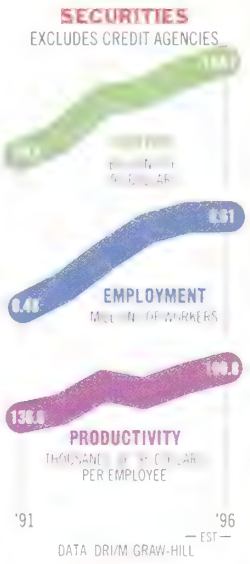
There are bright spots. Merrill Lynch, the biggest brokerage, sees continued growth in its retail business. Its equity assets under management have grown significantly in 1995 simply because the stock market was up 37%. This increase means more asset-management fee income in 1996, even if the growth of assets slows. And following a dismal 1995 in many emerging markets, Merrill is looking for an improvement in 1996.

The entire industry may get a boost from Washington. A capital-gains tax cut and a restoration of tax deductibility for individual retirement accounts look likely in 1996, says Marc E. Lackritz, president of the Securities Industry Assn., since "there is broad agreement among the House, the Senate, and the Administration that this is a good idea." The SIA estimates the IRA change alone could earn the industry as much as $200 million a year in additional IRA mutual-fund fees.

Of course, it's the unexpected that hurts markets the most, as in the last big market plunge with the gulf war in 1991. A recession or sharply higher rates are constant worries. But it now looks as if Wall Street can spend another happy year looking forward to bonus time.

By Leah Nathans Spiro in New York

PROGNOSIS '96



POSITIVES

- The soaring stock market is boosting the brokerage business.
- Mergers, acquisitions, and IPOs should remain strong.
- Congress may cut capital-gains taxes and restore deductibility of IRAs.

NEGATIVES

- Brokerage stocks are due for a correction after their big 1995 runup.
- Overcapacity in the industry will keep restraining margins.

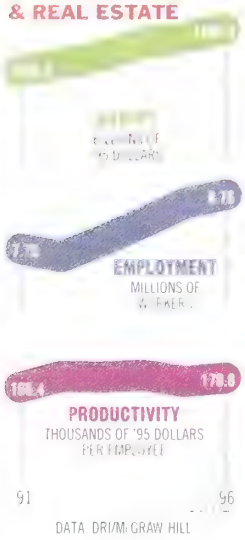
SPOTLIGHT

A YEAR OF HIGH-RISE EXPECTATIONS

THE OFFICE MARKET EXPECTS A BANNER YEAR, WHILE OTHER MARKETS LOOK LESS ROBUS

PROGNOSIS '96

CONSTRUCTION & REAL ESTATE



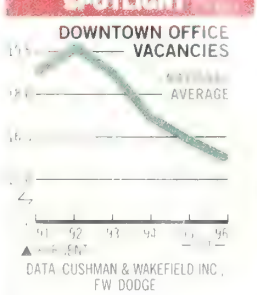
POSITIVES

- The office sector will continue to recover, thanks in part to strong demand by high-tech companies.
- Upscale hotels should enjoy rising room rates and healthy occupancy levels.

NEGATIVES

- Some shopping centers will feel the squeeze from a sluggish retail market.
- With apartment construction still picking up steam, some Sunbelt markets may already be overbuilt.

SPOTLIGHT



For much of the past two years, the real estate and construction industry celebrated the return of growth. Having survived the dark days of the early 1990s, investors savored the recovery of apartment and retail properties, followed by offices and hotels. But 1996 will be more of a mixed bag. On the downside, there are early signs of overheating in some markets for construction of apartment and retail space. On the upside, a stronger housing market should help pick up the slack. And with office occupancy and rents improving, 1996 will mark the return of one fixture of the 1980s: high-rise office projects.

The generally good news for real estate stems largely from the continued decline of interest rates. Lower rates helped spark homebuilding in the second half of 1995. And National Association of Home Builders Chief Economist David F. Seiders figures moderate economic growth will lead to even lower mortgage rates in 1996, averaging about 7.3% for 30-year fixed-rate mortgages. That should nudge multi- and single-family housing starts up about 3%, to nearly 1.4 million. The days of speculative boom and bust are gone: "People look at houses as shelter rather than as an investment strategy, and frankly that's pretty healthy," says Bruce E. Karatz, chairman of Los Angeles-based Kaufman & Broad Home Corp.

Apartment construction continues to pick up steam. According to the NAHB, construction will begin on 290,000 apartments in 1996, up a bit from 1995's 274,000. While that is still less than half the 1985 frenzied peak of nearly 670,000 units, industry pros are warning that some Sunbelt markets, such as Phoenix and Las Vegas, may already be overbuilt.

BANNER YEAR. In retail construction, megamerchants such as Wal-Mart Stores Inc. and Circuit City Stores Inc. are aggressively expanding. But it doesn't appear that the market is headed for a repeat of the overbuilding binge of the 1980s. Retail construction should fall 10% in 1996, according to The McGraw-Hill Companies' F.W. Dodge unit. One reason: Aside from the retail giants that can finance their own expansion, "capital is pretty well cut off to that sector," says Douglas A. Tibbetts, president of Equitable Real Estate Investment Management Inc.

Players in the office market expect 1996 to be a banner year. Thanks in no small pa the explosive growth of high-technology co nies, office vacancy rates continue to And the strength of the market is sparkin only build-to-suit construction but some pa ly speculative building in tight markets. A J. Mirante II, chief executive officer of C man & Wakefield Inc., says some cities see construction with as little as 50% o project pre-leased. "The fundamentals for haven't been this good in 10 years," Thomas A. Carr, president of Carr R Corp. in Washington, D.C.

Still, not all markets booming. Los Angeles downtown Dallas, whic a staggering vacancy ra 35%, are still struggling. Arthur Andersen & Co. aging Director Barry I bert warns that better cheaper telecommunica will allow more tenan the future to avoid dow locations. As a result, operators will be forc beef up their marketing improve the flexibilit lease packages.

Perhaps the best around remain high-end hotel properties. side of Las Vegas, there is little new cons tion of luxury hotels. And Japanese inve who overpaid for such properties in the continue to sell. A Japanese bank recently the 539-room Ritz Carlton Hotel, Mauna in Hawaii, built for $180 million, for jus million.

SMALL FAVORS. While the Japanese are ing, U.S. real estate continues to attract pension funds, which should cautiously e their holdings in 1996, as well as foreig vestors, from such places as Hong Kong wan, and Germany. Real estate invest trusts aren't raising a lot of money th public offerings—investment dollars have into the booming stock market instead they're discovering that private placemen work, too. For instance, Carr Realty str deal in November that will result in a million investment in the REIT by Security ital U.S. Realty. Carr plans to use the cap build and buy offices across the country.

1996 won't see a return to the glory d leaping prices. But these days, most re tate executives are thankful for slow but progress.

By Amy Barrett in Wash

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LOOKING FOR SAFETY IN NUMBERS

CONSOLIDATION—AND COMPETITION FROM OTHER INVESTMENTS—ARE CHANGING THE BUSINE

PROGNOSIS '96

INSURANCE

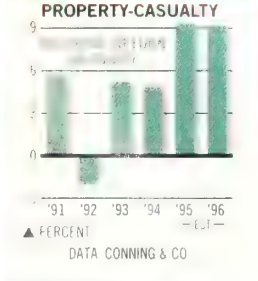
POSITIVES

- Life insurers are holding on to their share of retirement assets.
- Property-casualty writers are increasing reserves for environmental claims.
- Losses from claims are moderating.

NEGATIVES

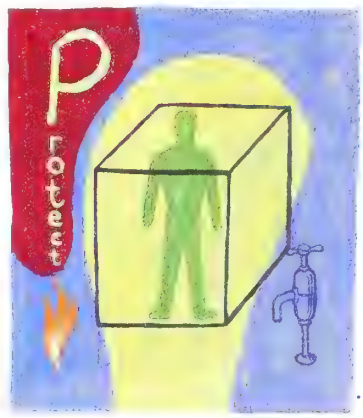
- Much of the industry's increased capital is coming from investment gains, not core earnings.
- With 2,400 competitors, the business is ripe for consolidation.

SPOTLIGHT



If there is one word that sums up prospects for the insurance industry in 1996, it's consolidation. Last year saw a record $18 billion worth of insurance-company mergers and acquisitions, and there's no letup in sight. "There are too many players competing for too little return in a crowded marketplace," says Eric Simpson, a vice-president at rating agency A. M. Best Co.

The late November announcement of Travelers Inc.'s $4 billion purchase of Aetna Life & Casualty's property-casualty unit capped a year in which CNA Financial swallowed Continental Insurance for $1.1 billion and Zurich Insurance took over Home Insurance. The same pressures that forced these deals—weak returns, large exposures to environmental claims, and lack of sufficient capital to keep ratings up—are expected to continue in 1996. While the companies have said nothing publicly, analysts believe that CIGNA Corp. and Prudential Insurance Co. are among the big-name companies considering selling their property and casualty units.



CUTTING OVERHEAD. For property-casualty insurers, two big helpers are low inflation and low interest rates. The benign operating environment in 1995 led to a doubling of net income, to $22.3 billion from $10.9 billion in 1994.

In 1996, however, property-casualty insurers should see only a modest uptick in their business. A survey of Wall Street analysts by Insurance Information Institute found them expecting growth in premium dollar volume of about 4.6% in 1996. While that would be better than the 3.9% rate of growth in 1995, it will still lag behind the growth of the early 1990s. The problem: continued price pressures from overcapacity, especially in commercial lines, such as general business liability and workers' compensation. "There has been no fundamental improvement in underlying performance during the last five years," says Robert Stein, director of Ernst & Young's insurance-industry practice.

With paltry premium growth, property-casualty insurers will have to cut overhead, now a quarter on every dollar of premium. Travelers hopes to trim $300 million from operating expenses and cut 3,000 jobs when it takes over the Aetna unit.

The consolidation trend affecting property-casualty writers is no less dramatic in life insurance. Metropolitan Life Insurance Co. New England Mutual Life Insurance Co. announced plans to merge, while several ators, such as General Electric Capital Ser Inc., went on buying sprees. Here, the mo tion is increasing assets under manageme compete with gargantuan mutual-fund ho and other financial-services conglomerates

EXPENSIVE DISTRIBUTION. Life insurers 1996 facing continued weakness in their business as more Americans turn away traditional life insurance to investment ucts such as mutual funds. While mutual are sold through low- consumer-oriented direct keting such as television insurers still sell their ucts mainly face-to through an expensive net of agents.

A survey by consu Towers Perrin found tha No. 1 issue of concern fo insurance chief executiv ficers is improving thei tribution system. To Perrin consultant Rick H estimates that distrib makes up two-thirds o cost of a life-insurance p "Traditional life companies have delegat their agents decisions like what mix of pro to sell, what markets to pick, and how to mote the products," says Berry. Many li surers have begun striking deals with b to sell their products, a trend that is like accelerate in 1996.

Insurers have had good results sellin nuities, which typically offer income or c gains as well as life insurance. The 13% r growth for annuities is four times the ra traditional life insurance products. But co tition is getting fierce. "It's a changing scape," says CNA Chairman and CEO Denn Chookaszian. "Banks will be a much mor nificant seller of these products in the futu positive for life insurers is that their mor and real estate problems of the early have largely dissipated, while strong fin markets have helped investment returns.

A couple of years back, few would have ined alliances such as Travelers' bold deal Aetna or life insurance companies allowing competitors in banking to sell their pro But as the historically underperforming i ance industry tries to catch up to the new order in financial services, it is learning to a

By Tim Smart in New Y

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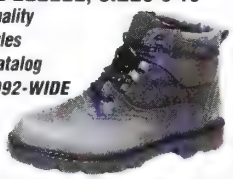

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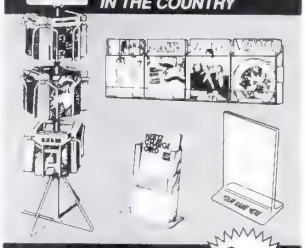

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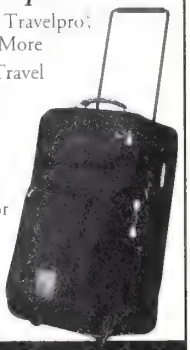

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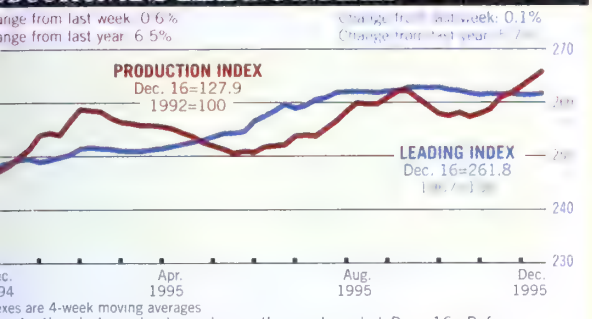
ODUCTION AND LEADING INDEXES



xes are 4-week moving averages

oduction index edged up during the week ended Dec. 16. Before ation of the four-week moving average, the index rose to 129.8, from . Increases in the seasonally adjusted output of autos, trucks, and ic power led the advance.

eading index was up slightly in the latest week. The unaveraged index ed to 262.4, from 263.1 in the previous week. Higher stock prices and bond yields are signaling solid economic growth ahead.

...dex ...yright 1996 by The McGraw-Hill Companies BW leading index ...yright 1996 by CIBCR

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (12/23) thous. of net tons	NA	1,798#	NA
AUTOS (12/23) units	133,174	141,894r#	-5.4
TRUCKS (12/23) units	112,949	122,358r#	4.1
ELECTRIC POWER (12/23) millions of kilowatt-hrs.	NA	64,899#	NA
CRUDE-OIL REFINING (12/23) thous. of bbl./day	NA	13,892#	NA
COAL (12/16) thous. of net tons	19,793#	19,438	-2.7
PAPERBOARD (12/16) thous. of tons	NA#	828.3	NA
PAPER (12/16) thous. of tons	NA#	800.0	NA
LUMBER (12/16) millions of ft.	404.4#	442.4	-19.1
RAIL FREIGHT (12/16) billions of ton-miles	24.6#	25.1	0.4

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA[1], SFPA[2], Association of American Railroads

DING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
K PRICES (12/22) S&P 500	609.42	618.65	32.8
ORATE BOND YIELD, Aaa (12/22)	6.88%	6.83%	-18.6
STRIAL MATERIALS PRICES (12/22)	111.4	112.3	-0.5
NESS FAILURES (12/15)	NA	333	NA
ESTATE LOANS (12/13) billions	$503.4	$503.9r	9.4
Y SUPPLY, M2 (12/11) billions	$3,735.7	$3,735.0r	4.5
AL CLAIMS, UNEMPLOYMENT (12/9) thous.	341	378	4.0

es: Center for International Business Cycle Research (CIBCR), Standard & Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures e companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on ss failures and real estate loans.

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (12/27) $/troy oz.	387.050	387.600	1.4
STEEL SCRAP (12/26) #1 heavy, $/ton	134.00	134.00	-6.6
COPPER (12/23) ¢/lb.	134.2	139.1	-4.4
ALUMINUM (12/23) ¢/lb.	79.0	79.0	-13.2
COTTON (12/23) strict low middling 1-1/16 in., ¢/lb.	80.35	83.84	-2.2
OIL (12/26) $/bbl.	19.26	19.12	9.2

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

EREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
RAL FUNDS (12/26)	5.50%	5.90%	5.60%
IERCIAL PAPER (12/26) 3-month	5.62	5.61	6.31
IFICATES OF DEPOSIT (12/27) 3-month	5.55	5.67	6.37
MORTGAGE (12/22) 30-year	7.46	7.45	9.34
STABLE MORTGAGE (12/22) one-year	5.60	5.70	6.73
E (12/27)	8.50	8.50	8.50

s: Federal Reserve, HSH Associates, Reuters Holdings PLC

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (12/27)	102.81	102.34	100.32
GERMAN MARK (12/27)	1.43	1.44	1.57
BRITISH POUND (12/27)	1.56	1.54	1.54
FRENCH FRANC (12/27)	4.89	4.95	5.43
ITALIAN LIRA (12/27)	1579.5	1589.8	1642.8
CANADIAN DOLLAR (12/27)	1.36	1.36	1.40
MEXICAN PESO (12/27)	7.635	7.560	4.975

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense ent. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

the prolonged Washington shut- all government release dates are to be postponed.

SURVEY

y, Jan. 2, 10 a.m. ▶ The National ation of Purchasing Management's ss activity index probably rose to in December, according to the forecast of economists surveyed by ternational, one of The McGraw-Hill nies. That low reading suggests that ustrial sector was struggling in ber. For the previous four months, M index slid below the 50% mark gnals a shrinking factory sector. The as 46.5% in November.

CONSTRUCTION SPENDING

Tuesday, Jan. 2, 10 a.m. ▶ The MMS survey expects that construction outlays probably dropped by about 0.5% in November, after jumping 2.7% in October. Following a surge in October, spending on public-works projects likely fell back in November.

NEW HOME SALES

Wednesday, Jan. 3, 10 a.m. ▶ New single-family homes probably sold at an annual rate of 675,000 in November, little changed from the 673,000 sales rate in October, says the MMS report. Home buying has declined for three consecutive months, but lower mortgage rates in 1996 could stabilize home sales in the first quarter.

FACTORY INVENTORIES

Thursday, Jan. 4, 10 a.m. ▶ Factory inventories probably grew by about 0.3% in November, after a 0.4% gain in October. That's suggested by the small increase in factory output for the month.

EMPLOYMENT

Friday, Jan. 5, 8:30 a.m. ▶ The MMS median forecast calls for a gain of 125,000 new nonfarm jobs in December, less than the 166,000 added in November. However, the survey also calls for manufacturing jobs to rise by 15,000, the first increase since August. The unemployment rate probably stood at 5.6% last month, unchanged from November's rate.

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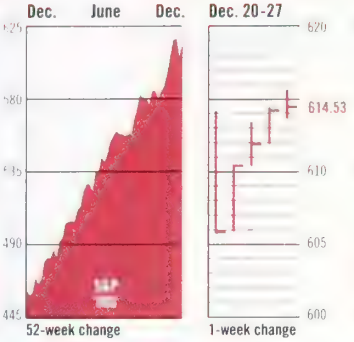
Business Week (ISSN 0007-7135) published weekly, except for one issue in Jan The McGraw-Hill Companies, Inc. Executive, Editorial, Circulation, and Advertising Office Avenue of the Americas, New York, N.Y. 10020. U.S. subscriber rate $49.95/year; Cana $69/year.Second-class postage paid at New York, N.Y., and at additional mailing offices. paid at Montreal, P.Q. Canada Post International Publications Mail Product Sales Agreem 246484 **Postmaster:** Send address changes to BUSINESS WEEK, P.O. Box 430, Hightstown, N.J.

vestment Figures of the Week

NTARY

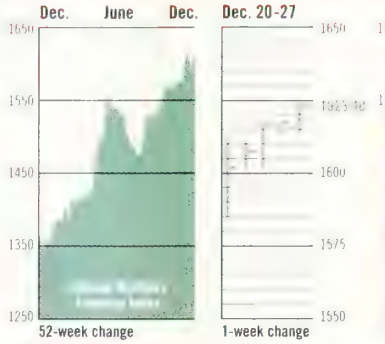
tock market's best year in ades drew to a close, in- took profits. After reaching f 5216.5 on Dec. 13, the ustrials fell as low as 5059 rebounded to 5106 on As expected, the Federal cut short-term interest it that didn't count for th bond buyers, who in- cused on the budget im- etween President Clinton GOP-controlled Congress. abroad, the long-ailing e and Mexican stock mar- ged yearend rallies.

STOCKS



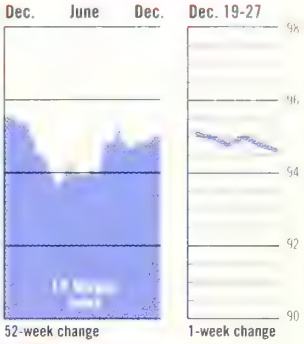
52-week change +33.3%
1-week change +0.4%

BONDS



52-week change +19.6%
1-week change +1.2%

THE DOLLAR



52-week change 3.3%
1-week change -0.4%

KET ANALYSIS

OCKS	Latest	% change Week	% change 52-week
ES INDUSTRIALS	5105.9	–0.1	33.0
COMPANIES (S&P MidCap Index)	216.4	2.1	28.6
OMPANIES (Russell 2000)	314.1	2.6	28.1
PANIES (Russell 3000)	350.5	0.9	33.1

N STOCKS	Latest	% change (local currency) Week	% change (local currency) 52-week
(FINANCIAL TIMES 100)	3676.4	2.8	18.8
IKKEI INDEX)	20,011.8	4.6	1.8
(TSE COMPOSITE)	4684.2	0.7	11.5

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.02%	5.22%	5.59%
30-YEAR TREASURY BOND YIELD	6.00%	6.10%	7.83%
S&P 500 DIVIDEND YIELD	2.23%	2.24%	2.79%
S&P 500 PRICE/EARNINGS RATIO	17.4	17.3	17.0

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	557.5	554.4	Positive
Stocks above 200-day moving average	64.0%	62.0%	Neutral
Speculative sentiment: Put/call ratio	0.56	0.72	Negative
Insider sentiment: Vickers sell/buy ratio	1.24	1.24	Positive

BLOOMBERG FINANCIAL MARKETS

USTRY GROUPS

NTH LEADERS	% change 1-month	% change 12-month	Strongest stock in group	% change 1-month	% change 12-month	Price
H CARE SERVICES	18.6	55.8	AMGEN	21.6	96.8	57 5/8
ND GAS DRILLING	18.4	33.8	ROWAN	24.2	54.0	9 5/8
S	10.7	66.6	ELI LILLY	15.2	73.2	56 1/2
ELL EQUIPMENT AND SERVICES	8.8	33.7	McDERMOTT INTERNATIONAL	22.4	–14.2	21 7/8
AL PRODUCTS	8.8	64.9	ST. JUDE MEDICAL	20.6	54.6	39 15/16

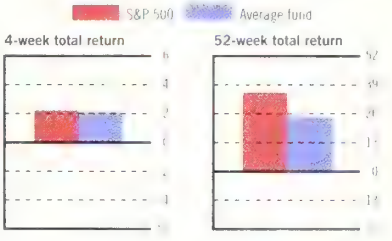
NTH LAGGARDS	% change 1-month	% change 12-month	Weakest stock in group	% change 1-month	% change 12-month	Price
NUM	–9.6	19.2	ALCOA	–11.2	22.4	51 1/2
ALTY APPAREL RETAILERS	–9.5	6.1	GAP	–13.8	38.5	41 3/8
AL MERCHANDISE CHAINS	–6.7	8.4	KMART	–18.8	–51.4	6 1/4
CONTAINERS	–6.7	–8.6	STONE CONTAINER	–9.8	–22.5	13 3/4
S	–6.1	7.0	ASARCO	–13.2	5.7	30 3/8

UAL FUNDS

MORNINGSTAR INC

S k total return	%	LAGGARDS Four-week total return	%
ITY SELECT ENERGY SERVICE	11.7	STEADMAN AMERICAN INDUSTRY	–5.8
REEN U.S. REAL ESTATE EQUITY Y	11.4	KEYSTONE AMERICA HARTWELL EMERG. GR. B	–5.4
IT EQUIFUND-MEXICO	11.4	AMERICAN PERFORMANCE AGGRESSIVE GRTH.	–5.4

total return	%	52-week total return	%
CAPITAL APPRECIATION	77.5	EV MARATHON GREATER INDIA	–33.2
TY SELECT ELECTRONICS	73.8	WRIGHT EQUIFUND-MEXICO	–32.3
T SMALLER COMPANIES A	72.4	STEADMAN TECHNOLOGY GROWTH	–28.0



TIVE PORTFOLIOS

lounts represent the alue of $10,000 one year ago ortfolio

ges indicate total returns

U.S. stocks	Treasury bonds	Foreign stocks	Money market fund	Gold
$13,678	$13,334	$12,030	$10,564	$10,198
+1.23%	+1.40%	+2.80%	+0.12%	+0.61%

this page are as of market close Wednesday, Dec. 27, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close Dec. 26. Mutual fund returns are as of Dec. 22. Relative portfolios are valued as of Dec. 26. A more detailed explanation of this page is available on request. r=revised

HOW TO EVALUATE TAX REFORM

This is shaping up as the year of America's great tax debate. About time. The U.S. tax system is a mess, riddled with exemptions, deductions, and credits that serve little purpose beyond rewarding favored constituents. The tax system is expensive for individuals and corporations to comply with, too.

Tax reform is already an issue in the Presidential race. A GOP commission headed by former Representative Jack F. Kemp will soon issue recommendations. All the main tax-writing committees plan to hold hearings on tax reform this year. To evaluate all the competing proposals for overhauling the byzantine tax code, ranging from a single income-tax rate to a national sales tax, we suggest a guide that's over 200 years old: *The Wealth of Nations*. Adam Smith laid out four maxims with regard to taxes in general: certainty, convenience of payment, economy in collection—and equality.

The flat tax is in the forefront of tax reform, and three of Smith's maxims—certainty, convenience of payment, and economy in collection—would be well served by a one-rate structure. The leading proponents of a flat tax are Hoover Institution economists Robert Hall and Alvin Rabushka, and their ideas powerfully shaped the flat-rate tax legislation of House Majority Leader Richard K. Armey (R-Tex.). Hall and Rabushka would levy a single 19% flat rate on wages and salaries; Armey wants to get the rate as low as 17%. There would be no deductions, though to keep the system somewhat progressive Hall and Rabushka exempt from income taxes $16,500 for a married couple and $4,500 a child. Capital g interest, and dividends would be exempt from taxes. nesses would lose many deductions, although invest spending would get an immediate 100% first-year tax w off. Business would pay a 19% rate on total income for Armey), after deducting wages, salaries, pensions costs of goods and materials. Bottom line: a highly simp and more efficient system where income gets taxed once as close as possible to its source.

Still, even with generous up-front exemptions, an a nothing one-rate tax is less progressive. In the past de global economic forces have increased income inequality. Americans have only one major asset to their name home they bought using generous tax incentives. Losin mortgage-interest deduction would squeeze the middle A flat tax raises other questions, such as ditching chari deductions and the deductibility of state and local taxes the federal government asks charities and local governm to assume more responsibilities. Perhaps a "modified," sti lined tax approach is called for, one based on two or rates and allowing for a few of the most justifiable deduc such as charitable contributions and home-mortgage int

The good news: The gale winds of creative tax re are sweeping Washington. Radical simplification would long way toward creating a less intrusive government more efficient economy. But some equity must be prese

DON'T TREAD ON FREE TRADE

What will the new year bring? An agreement between the White House and Congress to slash federal deficits for the rest of the century. Inflation will remain subdued, and since inflation powerfully influences the stock and bond markets, investors should enjoy decent returns. And, as our 1996 Industry Outlook makes clear (page 72), the U.S. economic expansion that began in 1991 should continue.

Of course, as in any forecast, a lot could go wrong. One particularly disturbing threat to continued growth lies with the virulent voices of economic reaction—protectionists such as Pat Buchanan and the rapidly expanding number of politicians who know better but make sympathetic noises to garner votes. The rallying cry of today's isolationists and their fellow travelers may be, "no more free-trade agreements"—not with Chile nor with anyone else. But what they are calling for, if heeded, would lead only to slower growth. Instead, policymakers should push hard for fewer trade barriers—and faster economic growth.

True enough, there are losers as well as winners from freer trade. But trade is not a zero-sum business. It's freer trade that helped slay the inflation dragon that terrorized the U.S. economy for much of the '70s and '80s. White-hot foreign competition is a key reason for disinflation fast bec the norm in the once inflation-prone U.S. economy. spurs growth by offering entrepreneurs and companies b markets. U.S. companies are getting more and more of sales overseas. Perhaps most important, freer trade en ages the creation and spread of new technologies and mercial ideas. In sharp contrast, steep trade barrier leave an economy stagnant. Look at Latin America for of the period after World War II—or the former S Union, for that matter.

Isolationists are far more powerful in Europe and than they are in the U.S. Many developing nations ar maneuvering to boost exports while protecting their market, too. It is more important than ever that the w remaining superpower provide free-trade leadership. I tumultuous period following the end of the cold wa most important decision made by the Bush and Clinto ministrations and Congress was to continue the free policies America has championed since 1945. This be paid enormous economic dividends in the 1990s. The b from trade and stronger economic ties among nations is tiful indeed.

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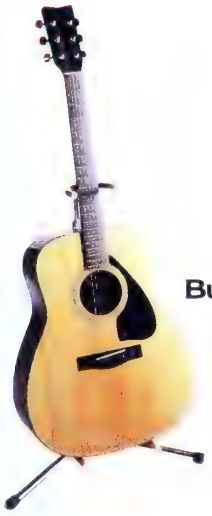

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SIC WHY AMERICA MAY LOSE ITS EDGE

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United Technologies

BusinessWeek

JANUARY 15, 1996

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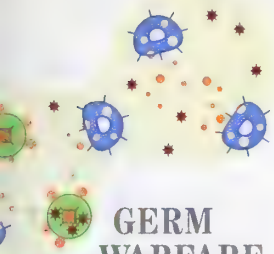

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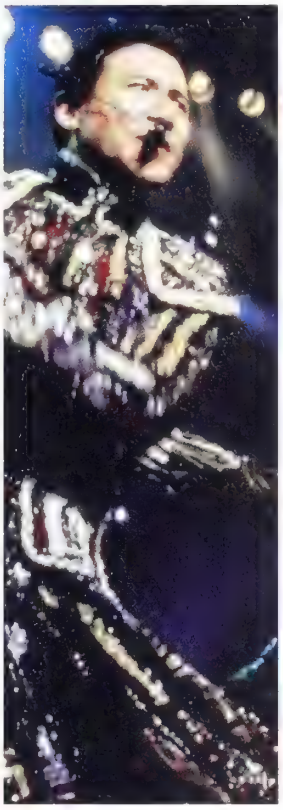

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Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

TALK SHOW "People blame everyone. There's no more gain in trying to blame the other side."

—Senator John Breaux (D-La.), exasperated as partisan gridlock continues over the federal budget

POLITICS AS USUAL

THE CORNER-OFFICE CANDIDATE

THE CORNER OFFICE THINKS the best Republican for the Oval Office is Bob Dole, by a vast margin. A survey of 401 senior executives drawn from the BUSINESS WEEK 1000 finds that 52% prefer the Senate majority leader as the 1996 GOP nominee. No. 2 is publisher Steve Forbes, at a distant 8%. After that, the list trails off: former Tennessee Governor Lamar Alexander (7%), Senator Richard Lugar of Indiana (6%), Senator Phil Gramm of Texas (5%), and commentator Pat Buchanan at a mere 1%.

BUSINESS MAN: *Dole 52%, Forbes 8%*

Dole's immense lead is even wider than his edge among Republicans generally. A recent Harris poll had the Kansan at 45%, with Gramm next at 9%, Buchanan at 6%, and Forbes at 6%. Harris, by the way, did the BW survey.

Assuming the inevitability of Dole's nomination—as he likes to—we asked the executives to pick between the senator and President Bill Clinton for the fall contest. No surprise here. The traditionally Republican group goes for Dole by 71%. Clinton scores just 19%. The blowout results change very little even if one of their own, a business type, enters the fray. Then, it's Dole 70%, Clinton 19%, Ross Perot 3%. □

CAPITAL OFFENSES

WHY LOBBYISTS AREN'T SWEATING

SO THIS IS LOBBYING REFORM? A bill to shed light on how Washington really works just became law. It forces thousands of behind-the-scenes influence peddlers—particularly lawyers, who have long claimed they didn't have to register—to tell who their clients are.

In some ways, though, the new law weakens existing restrictions. For instance, reps no longer have to identify the lawmakers they lobby. Also axed: requiring lobbyists for foreign companies to copy the Justice Dept. on letters they send legislators.

Even new gift-giving rules harbor plenty of loopholes. True, Congress in 1995 tightened up internal rules about gifts from Gucci Gulch. The House now bans all freebies except for nominal stuff such as a T-shirt. The Senate limits gifts to $50.

Don't think, though, that all this spells the end of those free three-martini lunches for lawmakers. Lobbyists already are dreaming up dodges. The senator is a golfer? One lawyer suggests there will be games of "loser pays" with lobbyists—who would always lose. Or restaurants could double their prices but offer two-for-one deals to lure lobbyists who would pay for lawmakers.

Penalties also are watered down under the new law. Lobbying violations used to be criminal. Now, miscreants face only civil fines. And the gift curbs will be enforced by the Hill's weak-kneed ethics panels. *Stan Crock*

THE LIST **THEY'RE THE TOP**

General Electric continues its reign as the top U.S. company in market value. In 1993, it wrested the honor from Exxon. An expanding economy in 1995 benefited GE's manufacturing and financial-services activities. 1995's top four companies were unchanged from '94. Among the top 10, the biggest gainer was Merck, jumping two places to No. 5. In a good year for drugmakers, its market cap surged 70%.

MARKET CAPITALIZATION

COMPANY (12/31/94 RANK)	12/31/95 (billions)
1 GENERAL ELECTRIC (1)	$120
2 AT&T (2)	103
3 EXXON (3)	101
4 COCA-COLA (4)	93
5 MERCK (7)	81
6 PHILIP MORRIS (5)	75
7 PROCTER & GAMBLE (9)	57
8 JOHNSON & JOHNSON (12)	55
9 MICROSOFT (11)	52
10 WAL-MART STORES (6)	51

DATA: STANDARD & POOR'S COMPUSTAT A DIVISION OF THE McGRAW-HILL COMPANIES

PROFIT & GLOSS

SORRY, WRONG NUMBERS

MISCOMMUNICATION AND finger-pointing on Wall Street have taken Barnes & Noble stock on a wild ride lately. The odd tale starts on Dec. 28, when PaineWebber Group analyst Craig Bibb raised his rating on the book chain to "buy" and the stock shot up 4.9%, from 30⅞ to 32⅜. The next day, Bibb abruptly lowered his rating to "neutral." The shares plummeted 10.4%, to 29.

MISREAD: *Barnes & Noble*

Wall Street analysts say Barnes & Noble CFO Irene Miller told them Bibb upgraded the stock without making the standard call to B&N to check his numbers. PaineWebber people, though, privately dispute Miller, saying Bibb phoned Miller twice between Dec. 13 and Dec. 28—calls that went unreturned, since she was vacationing part of that time. B&N traditionally won't discuss the crucial December sales figures early.

Bibb, in his rosy Dec. 2 report, predicted fourth-quarter sales growth at B&N superstores would be 7% to 9%. After Miller called to question his conclusion, Bibb the next day predicted growth of 3% to 6%, stating that he had just heard more about weak book sales in the Northeast. PaineWebber sources say Bibb's first forecast 7% to 9% growth in a Dec. 13 report, faxed to Miller's office; it received no response. Bibb, PaineWebber and B&N declined to comment publicly. *Willy Stern*

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Up Front

HEADS OR TAILS? *Only $6 a pound*

EDIBLES

EAT YOU LATER, ALLIGATOR

HERE'S QUITE A TOOTHSOME delicacy: alligator meat, which is finding its way onto more plates in the U. S. and Western Europe. Used to be that gators were used only for shoes and handbags. But the folks in the $28 million alligator biz have lost patience with fluctuating, unpredictable fashion dictates.

So the gator people have launched major promotions of their edibles over the past few years, setting up booths at restaurant-industry conventions for taste tests. "Specialty suppliers are always looking for something new," says a delighted Edwin Bradford, president of V.I.S., a gator-product outfit in Mandeville, La. The slogan for the alligator abattoir industry is: "The other, other white meat."

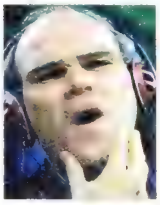
To better meet demand, gators are increasingly farmed, not hunted in the wild. The industry has even been able to surmount the loss of a major customer. Taiwan banned imports of American wildlife products in a 1993 trade tiff.

Demand in the American South and in European countries such as Britain and Finland has more than doubled the price of gator meat over the past three years. A pound of the stuff costs $4 to $6, more than the best cut of pork, which tastes somewhat similar. *Kate Murphy*

AFTERLIVES

FROM SUPER TUESDAY TO SUPER BOWL

POLITICS IS A LOT LIKE SPORTS. No surprise, then, that Democratic political mastermind James Carville is spending time these days handicapping football games. After all, he lost his standing as Bill Clinton's top political adviser to Dick Morris, and his role in the 1996 campaign is still unclear.



CARVILLE: *Calling 'em*

Carville is doing a weekly pigskin forecast for Washington radio station WTEM-AM, picking college and National Football League games. The sports talk show is hosted by Carville friend and *Washington Post* columnist Tony Kornheiser. Known in political circles as the Ragin' Cajun, Carville got a new nickname from Kornheiser: the Swami.

Why football? "I'm too old to talk about sex, so what else is there but sports and politics?" Carville replies. The Louisiana native—a diehard Louisiana State University fan—says he doesn't bet himself and doesn't get paid for his five-minute spots.

After a 0-5 start last fall, Carville called 17 of the next 25 games right. Carville erred by predicting that Florida wouldn't cover the spread against Arkansas, but he accurately picked the Indianapolis Colts' upset of the San Francisco 49ers. How about a new moniker: Jimmy the Cajun? *Dean Foust*

DRAWN & QUARTERED

ON THE LAM

AND NOW, THE IMMUNITY ISLANDS

TOO BAD FOR ROBERT VESCO. The Republic of Seychelles is offering to grant immunity and protection from extradition for anyone who invests $10 million in its economy. Had financier Vesco known, he could be free today. Last spring, Cuba got fed up with harboring Vesco and arrested him on undisclosed charges. The U.S. Justice Dept. is seeking Vesco's extradition.

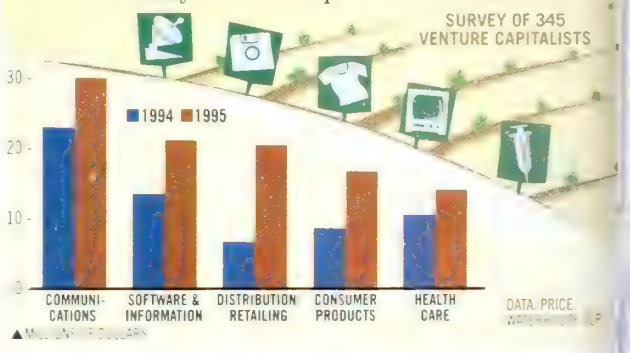
Meanwhile, the State Dept. and several European nations have complained to the Seychelles that its recent invitation will only attract embezzlers and other big-time crooks. Officials of the Indian Ocean island chain (population: 72,000), who claim that this isn't their intent, are facing the loss within a year of the islands' multimillion-dollar rental income from a U.S. Air Force tracking station.

In addition to legal safe haven, newcomers bearing fat wallets are guaranteed swift immigration clearance. It's too early to tell how many, any, criminals will come to the Seychelles. After all, some places, such as Brazil and Argentina, already have reputations as havens for well-heeled fugitives, but they don't make it their official policy. *Paul Magnusson*

THE BIG PICTURE

WHERE THE STARTUP CASH WENT

The lure of getting in early produced a flood of venture capital in 1995. Here are the top five industry segments for seed money in the third quarter of 1994 and 1995.



FOOTNOTES Unit sales of CD-ROM software worldwide: 1994, 92 million; 1995, 206 million

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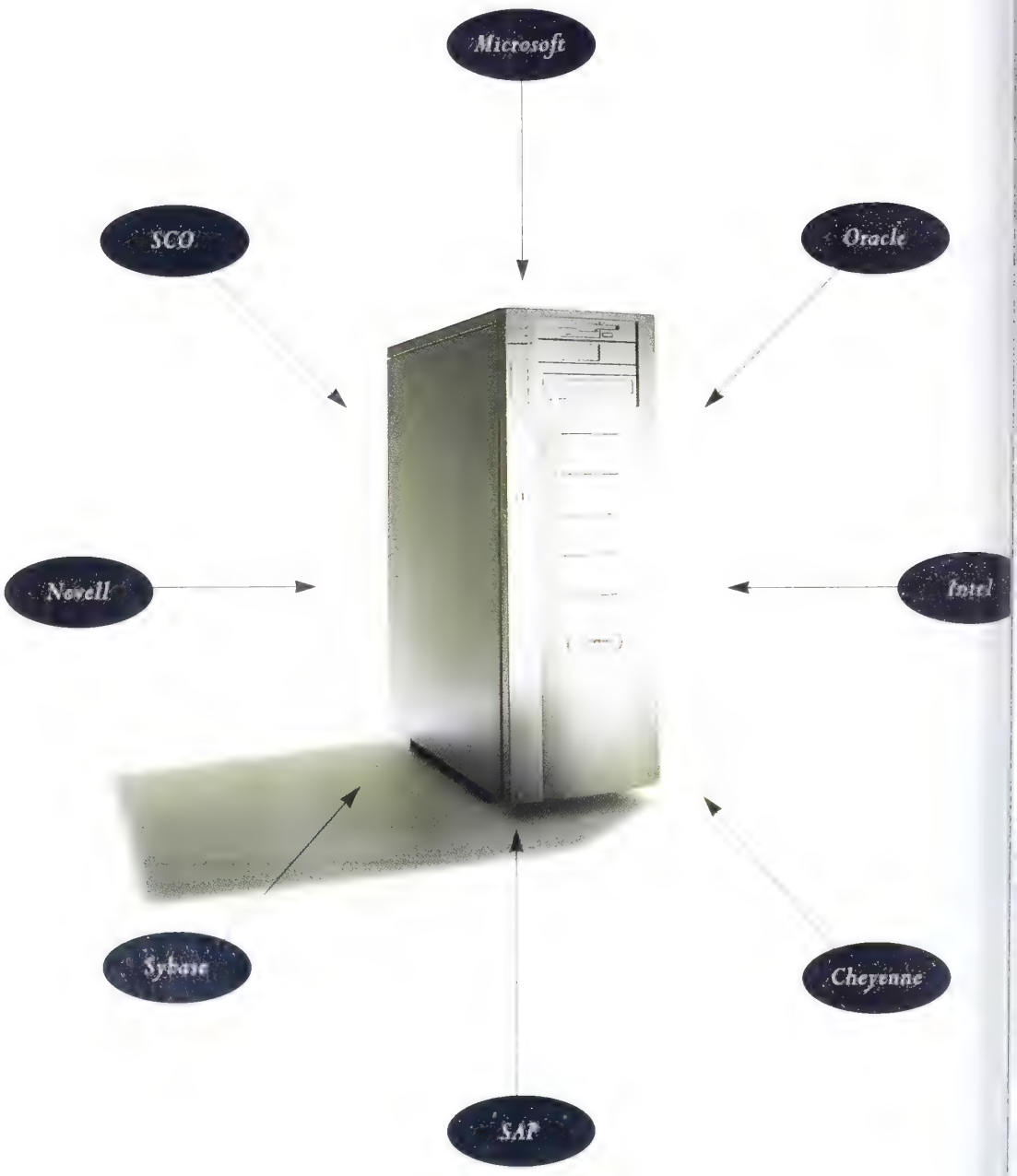

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You see, they may be Compaq servers. But they are Compaq-Microsoft-Oracle-SAP-Intel-Novell-SCO-Sybase-Cheyenne solutions. (We just couldn't fit all those logos on them.)

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Readers Report

IPOs CAN QUICKLY LOSE THEIR INITIAL CHARM

We noted with interest "The boom in IPOs" (Cover Story, Dec. 18), which recounted examples of wondrously successful initial public offerings of common stock. We would like to serve as wet blankets.

The issue for investors is whether those buying stock in these offerings actually do better than they would if they bought seasoned common stock, already public for several years. The answer: While in some cases they certainly do, in aggregate they do not.

You correctly noted that IPOs tend to jump in price during their first day of trading—and that stock bought after the initial jump tends not to be a good investment in the long run. But you also concluded, or at least suggested, that IPOs are good investments if bought before the jump. That is true only if you sell soon at the higher price. If you hold for five years, you will likely do worse than if you had bought seasoned stock. On average, you will still make a profit, but not as much as you would have in seasoned stocks.

Jonathan A. Shayne
President
Shayne & Co.
Nashville

Larry D. Soderquist
Director of the Corporate & Securities Law Institute
Vanderbilt University
Nashville

START THOSE ALASKAN DRILLS

I'm glad your story on the opening of the Arctic National Wildlife Refuge (ANWR) was a Commentary, because it ignored the factual arguments for opening the ANWR ("High noon on the Alaskan tundra," News: Analysis & Commentary, Dec. 11). It never mentioned that in 10 years—the time it will take to tap the Arctic coastal plain's oil in an environmentally safe way—America will need the oil. It never mentio
that oil production from Prudhoe Ba
declining by 4% to 5% a year and t
America will likely be dependent on f
eign sources for 75% of its oil by 20
as opposed to 51% now.

It certainly never mentioned that
tiny "footprint" of development—j
2,000 acres out of the 19 million-a
refuge—will have almost no effect
the calving grounds or migration rou
of the Porcupine caribou herd, u
which the Gwich'in Indians depend. N
is there any evidence that it will ha
any other species in Alaska. Any fair
view will show that oil exploration
occur without damage to the envir
ment and with significant benefit.

Frank H. Murkowski (R-Alas
Chairman, Senate Energy
Natural Resources Commit
Washing

A LUMP OF COAL IN OREGON'S STOCKING

The larger part of the story
missing in "Yuletide bounty in Oreg
(Economic Trends, Dec. 18). While
true that individual taxpayers receive
"present" of about $100 each beca
of our kicker law, that represented
about 6.27% of our state tax bills.
same law put something under the t
for corporations, too: More than hal
their state income-tax liability.

Meanwhile, our state universi
have high tuition, large classes, and
duced course offerings. Schools conti
to suffer from a 1990 Prop. 13-cl
property-tax-limitation measure. The
derly, the mentally ill, and children
need are not getting the help they
serve. This Yuletide bounty looks m
and more like a lump of coal.

Bentley B. Gilbert
Salem, O

WHO ELSE IS GUNNING FOR SOFTWARE'S GOLIATH?

I generally like your coverage of
software industry. But there are ti
when I think you go too far in y

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JANUARY 15, 1996 (ISSN 0007-7135)*** 3458

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Postmaster Send address changes to BUSINESS WEEK, P.O. Box 430, Hightstown, N.J. 08520. Second-class postage paid at New York, N.Y., and at additional mailing offices. Postage paid at Montreal, P.Q. Canada Post International Publications Mail Product Sales Agreement No. 246484.

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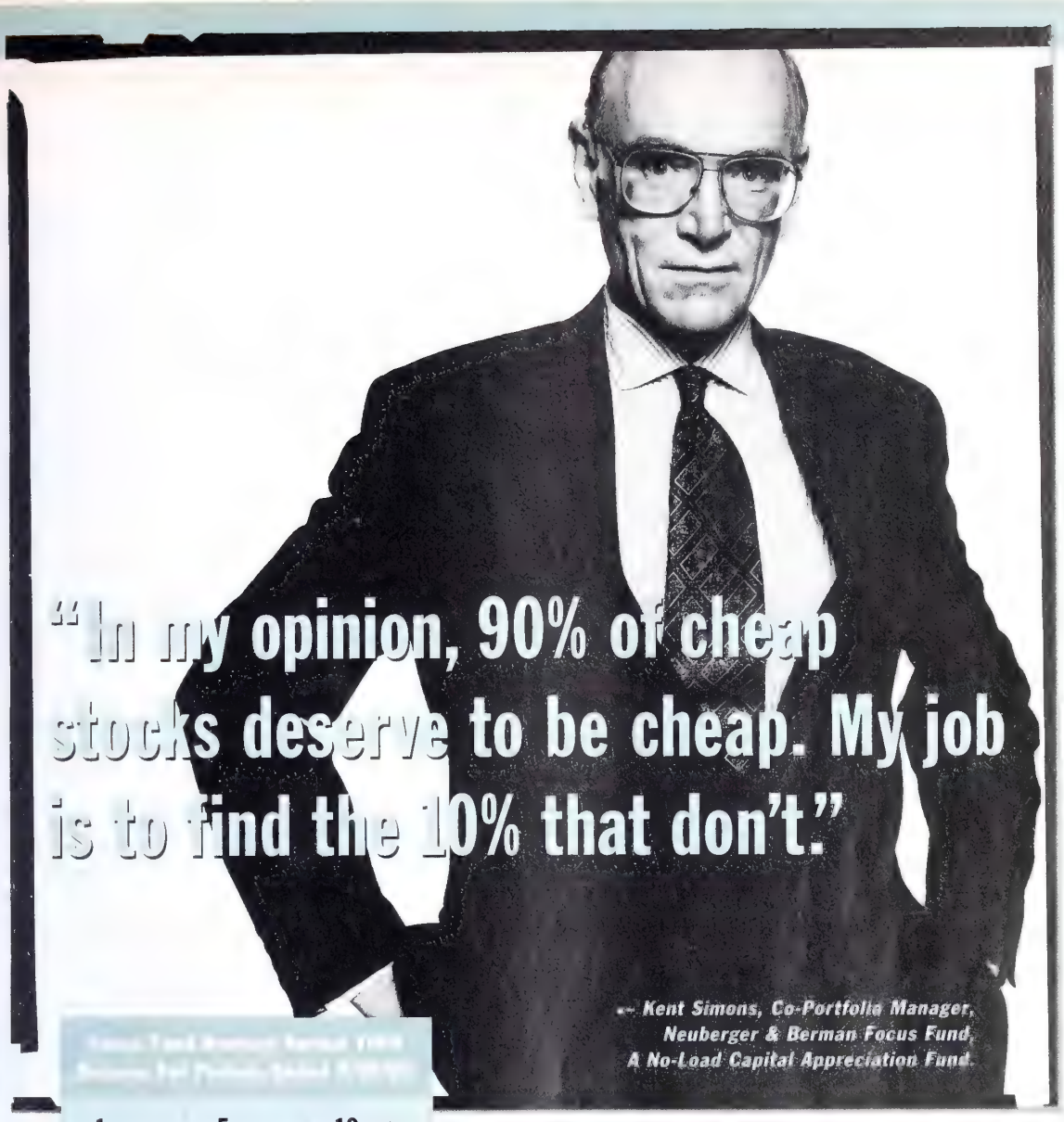

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forecasts. That's the case in some of the recent articles that you published concerning the Web and Java language ("The software revolution," Cover Story, Dec. 4, and "Win 95, lose '96?", News: Analysis & Commentary, Dec. 18) and how they threaten the Microsoft empire.

As a computer programmer, I don't like the way Microsoft handles the software industry. It has the bad habit of announcing the impending release of nonexistent software in some-quarter-of-next-year, just in order to keep its competitors away.

But to say that Sun Microsystems Inc. and Netscape Communications Corp. are in the running to unseat Microsoft with Java is a long shot. Java is still in its development stage, and the implementation of the Java virtual machine in the Netscape browser (version 2.0 beta) is slow.

The illustration of the red arrow pointing to the Help button in your article shows that maybe [Microsoft Chairman] Bill Gates is right: The media are looking hard for some small David to defeat the giant.

Omar Reis
São Paulo

THE MISPLACED 'REVENGE' OF VIRGINIA THOMAS

In "Revenge of the justice's wife" (Up Front, Dec. 18), you chortle about the "sweet revenge" being enjoyed by Virginia Thomas, wife of Supreme Court Justice Clarence Thomas. She is working hard to win passage of a bill that would restrict lobbying by nonprofit groups that receive federal funds. The supposed revenge is against those groups that "savaged her husband's court nomination." Only two such groups are cited—and one of them happens to be the ACLU.

This citation is wrong on two counts: The American Civil Liberties Union expressly took no position on the Clarence Thomas nomination; and the bill, if it passes, will not affect the ACLU because we have never received and would never accept federal funds. So for anyone seeking "sweet revenge," eat your heart out!

More important, the bill, even if it passes, is unconstitutional, and we will join in efforts to challenge it, as will many conservative not-for-profit groups that would be equally injured by it. As for Justice Thomas, he may need to recuse himself if such a case should rea
the Supreme Court, given his wife's
dent role.

Ira Glass
Executive Direct
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New Yo

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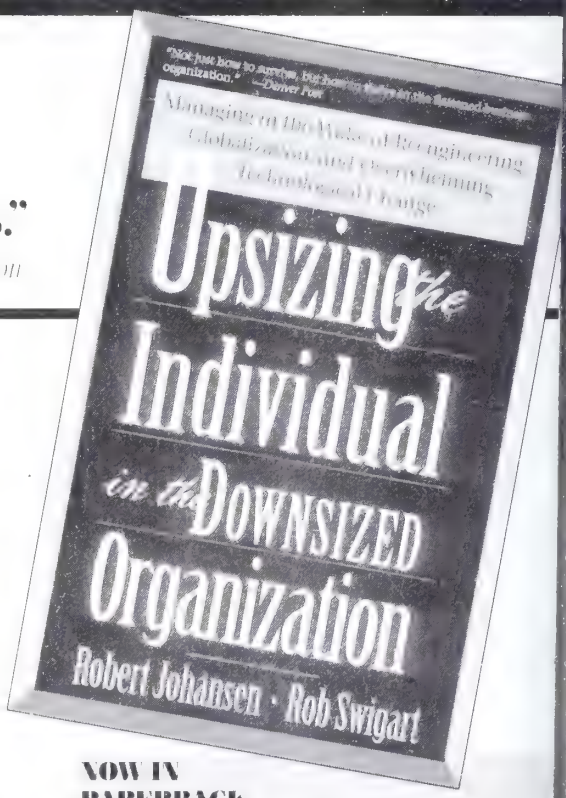

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TOTAL RISK
Nick Leeson and the Fall of Barings Bank
By Judith H. Rawnsley
HarperBusiness • 206pp • $24

THE SINGAPORE SLINGER: A CAUTIONARY TALE

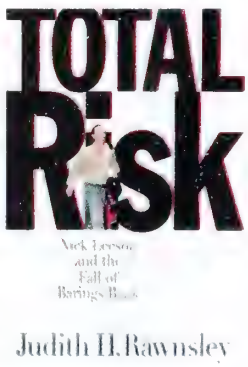
Let's get one thing straight. Nick Leeson, the 28-year-old futures trader now serving 6½ years in Singapore's Changi jail, did not bring down Barings PLC. That dubious distinction goes to six top executives and four sleepy outside directors. All chose not to see the dangers lurking in the hell-for-leather atmosphere at Baring Securities Ltd., the trading arm of the much older merchant bank known as Baring Brothers. When willful blindness joined forces with an almost total lack of management controls, all the conditions were in place to produce a Nick Leeson.

This is the crux of Judith H. Rawnsley's *Total Risk*, which exchange regulators, bank supervisors, and dealing-room managers worldwide should study. Her finding of institutional incompetence is in agreement with the conclusions of both Singapore authorities and the Bank of England—but Rawnsley offers a more stimulating read than either of their dense investigative tomes.

Rawnsley's account of Leeson's last day on the job is riveting. By January, 1995, he was frantic to make up for accumulated losses of $320 million. He began using Barings' funds to gamble—his particular bets were "straddles"—that the Nikkei stock index would trade within a narrow range between 19,000 and 21,000. But he was undone by the Jan. 17 Kobe earthquake that killed 5,000 people and sent the Nikkei plummeting. By Feb. 23, losses of $1.3 billion were taking a toll on his nerves—and his stomach. He had to leave the trading floor to throw up in the bathroom. "For once, everyone in the market had been right, except him," Rawnsley writes. He left the office after lunch, having been confronted by two senior officials about strange goings-on with his accounts, and never came back.

Most of this book isn't about Leeson, however. It's about the ignorance and colossal mistakes of senior executives. When Leeson arrived in Singapore in 1992 to help out with settlement of derivatives trades, no one knew to whom he reported. Soon, he was executing in-house as well as client orders from several other offices, particularly Tokyo, making it impossible for supervisors to check on him. A warning from James Bax, then head of the Asian regional office, that lack of accountability could lead to disaster went unanswered.

When rumors reached London in late 1994 that Leeson held very large Nikkei futures positions, senior officials blithely assumed the trades were on behalf of hedge-fund clients, a misconception that Leeson encouraged. Conflicts of interest abounded: Leeson was allowed both to make trades and settle them. Such an arrangement practically invites the creation of fictitious accounts to cover large trading losses, at least until the situation improves. Although Leeson hasn't tried to explain his actions, Rawnsley believes this is how his deception began. Then, when the market didn't move in his favor, he began doubling his bets in desperation.



But more was at work than a lack of supervision, Rawnsley says. A former *Euromoney* and *Economist Intelligence Unit* correspondent, the author had been a colleague of Leeson's from 1989 to 1992, when she was employed in Barings' Tokyo office. This background leads her to conclude that the disaster was the byproduct of a foolish strategy: Leeson and other young traders were expected to produce disproportionately huge profits from a tiny capital base. And Leeson desperately wanted to please his bosses as well as boost his own economic and social standing.

By the end of 1994, Leeson's trades were doing just that: He claimed to ha made $30 million, or nearly 20% of t year's total profit of $157 million. In ality, Leeson lost $285 million in th year. Meanwhile, the bank's total capi base—shareholders' funds and debt ca ital—stood at just $800 million. Leeso bogus claims went undetected, sa Rawnsley, because to question his me ods, or check his math, might ha slowed down Barings' aggressive glo expansion and reduced everybody's a nual bonus.

More fundamental, Rawnsley says, w that Barings had two very different c porate cultures. Conservative, traditi bound corporate financiers held sway Baring Brothers. But at Baring Secu ties, which didn't exist until 1984, F East experts, equity traders, and futu traders ran amok, far from Londo reach. And since Baring Securities p vided two-thirds of the bank's total pr it, cooler heads at Baring Brothers w reluctant to interfere. Finally, in 19 plans were laid to comb the two entities—but by t time, Leeson's paper-pr factory was in full swing.

Even so, several peo at Barings began sound alarm bells, and some these resulted in inter and external audits of Singapore slinger. These dits should have oper doors and led officials to ror Account 88888, i which Leeson dumped all trading losses. But executives were distracted by restructuring and int cated by visions of expected huge an bonuses to pin him down.

Today, Leeson is behind bars, but Barings fiasco isn't over. Asia head and his deputy, Simon Jones, may face prosecution by Singapore auth ties. In London, former board memb wait to hear whether they will be fo er barred from serving as director an investment bank. Such a ruling r be in order. But it's more critical banks to realize that destructive beha can be a byproduct of the macho phasis on maximum returns, and t strict controls are the only safegu The alternative is total risk.

BY PAULA DW

Dwyer is BUSINESS WEEK's Lon bureau chief.

THE WILLFUL BLINDNESS OF THE 10 BARINGS DIRECTORS LED TO THE FIASCO, SAYS RAWNSLEY

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wanted the whole experience to be like the park itself. It's been called a shrine to the game of baseball. it is absolutely New England," John Buckley of the Boston Red Sox recalled. John added, "The food had to ance the experience. That's all we said. That was our direction. And they took off from there. Before we knew e were all talking one-on-one with loyal Red Sox fans. A ton of ideas followed. New ways of doing things. were grilling chicken and selling it all. The chowder was receiving rave reviews. And all of it – every idea they – fit perfectly at Fenway." At ARAMARK, we believe pre-packaged solutions would be fine if there were such ing as pre-packaged problems. Instead, we learn our partners' business. And we help them pursue their ms and goals with an attitude absent of limits. It's moved John to also say, "Last year they helped us increase by [illegible]. Second in the league. But all they can say is 'Wait 'til next year.'"

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BY STEPHEN H. WILDSTROM

WANTED: A PC FOR THE MASSES

When last fall's sales are toted up, we're likely to find that just over a third of U.S. households now have computers. The computer industry fondly hopes that, someday soon, the PC will become as common as the microwave oven or the VCR. But to make that happen, the industry has got to roll up its sleeves.

Two factors keep computers out of many homes: cost and complexity. The first problem is rapidly taking care of itself, but removing the complexity requires rethinking the home computer.

What sort of machine would get PCs into the tens of millions of homes that don't have one yet? What's needed is much less a breakthrough in technology than a change in industry attitudes. Computers are a bit like cars in the 1920s: You no longer have to hire a mechanic to ride along with you, but you're still expected to get out and get under the hood once in a while. This has spawned a how-to book industry and—judging by my mail—lots of frustration even among the technically savvy.

COMPLEX BEASTS. The key to a true mass-market computer is its reliability and ease of use—not power and features. Even today's Apple Macintosh, let alone the typical Windows machine, won't do. For computers to become as ubiquitous as toasters, they have to be as easy to use.

And as reliable. That's why consumers need a crash-proof operating system, with crash-proof software to run on it. This may not be as hard as it sounds. Microsoft Corp.'s Windows NT and IBM's OS/2 both are very stable, partly because they do not have intricate routines designed to make them work with every piece of software ever written. Windows 95, while an improvement on its predecessor, still crashes distressingly often. And it presents users with too many ways to do things: Four different methods to move a file from a hard drive to a floppy adds confusion, not convenience.

In their present forms, Windows NT and OS/2 are complex beasts, not intended for novice home users. But their stripped-down technology could be the basis of the simple, bulletproof operating system for the mass-market computer.

The same design philosophy—simple and unbreakable—should apply to all the applications designed for these systems. While paying lip service to ease of use, software developers have engaged in a mad race to load on ever more features, layering them with "tips," "wizards," and "coaches" designed to unravel the mystery of their use. Some word processors even come with templates that provide all the text of a letter—you just add the address. But most people have little trouble writing their own letters; they need help using the software itself.

Software publishers insist that consumers want the latest and greatest and that simple just doesn't sell. "We tried selling mini word processors," says Chris Peters, who heads Microsoft's Office product unit. "They were spectacularly unsuccessful." But I don't think the concept of an easy-to-use word processor for home use has been given a fair trial.

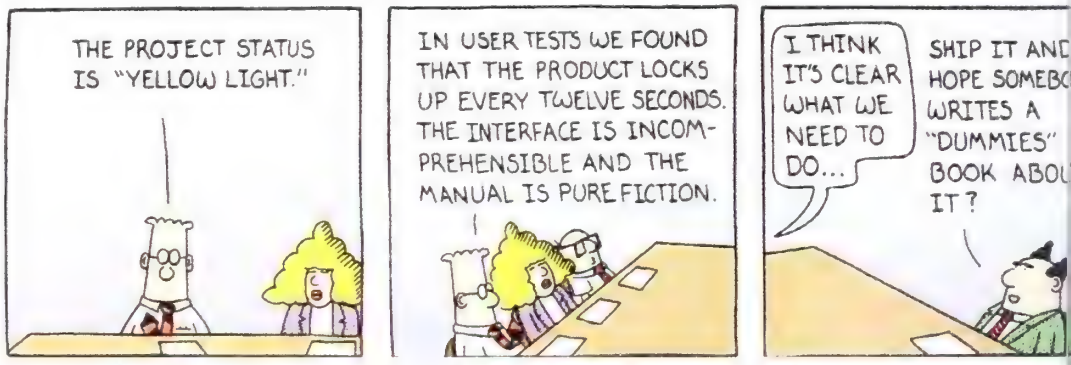
This home machine should come with a carefully chosen set of simple, solid applications loaded and configured. No need to worry about compatibility with old hardware and software: People buying their first computers don't have any.

Having crash-proofed the software, why not get rid of that wait of several minutes every time the PC goes through its mysterious, failure-prone ritual of booting up? You don't boot up your juicer or even your video game system, so who wants to wait on their PC?

IDLE MOMENTS. Fortunately, the remedial technology is at hand. I have a Hewlett-Packard OmniBook laptop that doesn't boot when I turn it on. Its secret: The power switch and a continuous trickle of electricity puts the computer into a deep sleep instead of turning it off, so that hitting the switch again causes it to wake up instantly with the screen just as I left it. Energy-saving technology already built into new computers can do most of the job—and with some rethinking of the power switch to make potential buyers feel at ease.

Manufacturers have already made strides in building user-friendly hardware. Such steps as color-coding cables simplify the job of setting up a PC. The much-talked-about $500 Internet machine could be just the ticket for Net surfers. Consuming data connections in the home become faster, cheaper, and more reliable, and that the Net offers more content that appeals to people who don't now own PCs.

Sure, the resulting computers may be less powerful as the industry measures such things, and will sacrifice the ability to work with nearly every peripheral and program ever designed. But making computers more user-friendly could make consumers more friendly to computers.



Reliability and ease of use—not power and features—are the ticket at home

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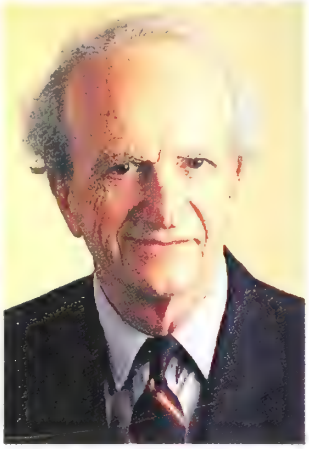
BY GARY S. BECKER

RELIGIONS THRIVE IN A FREE MARKET, TOO



RIVALRY: Competition benefits religious groups because they're forced to learn how to satisfy the needs of their members

Many people are disturbed by the rising appeal of the religious right. But I don't believe there is reason to be concerned—so long as religions must compete for followers and no religion receives special treatment from the government.

In a competitive environment, born-again Christians, Orthodox Jews, fundamentalist Moslems, and other groups attract members only if they meet spiritual and moral needs better than mainline religions. Most people believe individuals have the power to determine their lifestyles even when they grow up under difficult circumstances. They expect religious preaching to reaffirm their need to take responsibility for their behavior. With mainline religions failing to stress the need for people to exercise self-control and responsibility, they are losing members to fundamentalist groups with more traditional teachings. Fundamentalists also have been in the forefront of attacking the breakdown of the family, pornography, and disrespect for authority.

Some nations, such as the U.S., have an open "market" for religion. Different denominations and sects compete for members through spiritual guidance and other appeals. Competition is good for religion, as it is for ordinary commodities, because religious groups are forced to learn how better to satisfy members' needs than they do when they have a monopoly position.

ON THEIR TOES. The importance of competition to the behavior of religious organizations was recognized 200 years ago by Adam Smith in a neglected chapter of his *Wealth of Nations*. He presented considerable evidence that the Church of England had become unresponsive to the needs of the British because the government gave it a privileged position. Smith argued forcefully that the only way to end church leaders' sloth and indifference was to remove these privileges and make the Church of England compete for members against the newer religions.

Thomas Jefferson and other founders of the U.S. understood that church and state should be separate in the new nation. The First Amendment states that "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof." One reason for the separation of church and state is to force religions to remain on their toes as they compete for congregants.

Lawrence Iannoccone of Santa Clara University tested the Smith-Jefferson doctri with evidence on the degree of religiosi among the Protestant nations of Europe a North America. He found that religion—me sured by the number of regular churchgoe and the strength of religious beliefs—w more important to people in societies wi many competing churches, compared wi countries that have a single church. For stance, only a small percentage of the po lation in Scandinavian countries is interest in religion, in large part because the Luth an Church has a privileged position and ceives most of its financing from governme (though church and state are starting to s arate in Sweden). By contrast, religion thri in the U.S. because different sects and nominations compete fiercely for members

COMMUNIST SUPPRESSION. The Catho Church is losing its powerful monopoly po tion in South America, and fundamental Protestant sects are growing rapidly in place, because too many priests have ignor spiritual needs while focusing on politi goals. And prior to World War II, Japa government subsidized Shintoism and d criminated against other religions. The p tected position of Shintoism was abolish after the war, and hundreds of new grou are flourishing now in Japan. These grou have appealed to spiritual needs that app ently were not being satisfied by Shintois

No modern example shows the compe tive appeal of religion better than what happening in the onetime communist natio of Eastern Europe and the former Sov Union. For almost 75 years, the Soviet Un tried to reduce opposition to communism closing churches and imprisoning religi leaders. In essence, communism tried to tablish a secular monopoly. Yet religion been booming since the collapse of comm nism. More than 22% of Russians intervie say they used to be atheists, but they n believe in God. More than 6,000 Russian thodox churches and monasteries have opened, and many other religious organi tions have begun to recruit members the

These examples indicate that both libe and strict religious groups are more dyna when they have to compete for members o level playing field. Healthy competition quires open markets for religious beli where no religious organization receives s cial protection or privileges from the stat

Gary S. Becker, the 1992 Nobel laureate, teaches at the University of Chicago and is a Fellow of the Hoover Institution

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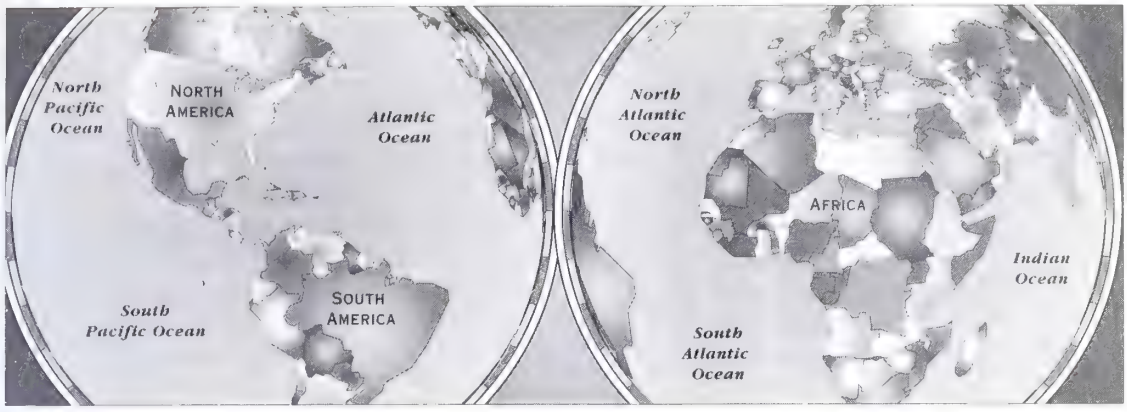

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BY GENE KORETZ

U.S. LABOR GETS FLEXIBLE...

Long-term jobs are waning

Two recent surveys underscore an ongoing debate about one of the most controversial U.S. labor market trends—the degree to which traditional work schemes offering regular long-term jobs are being replaced by more flexible, "contingent" arrangements under which workers are hired on a temporary or sporadic basis.

According to a detailed Conference Board canvass of some 93 major multinational companies, mostly U.S.-based, employment of contingent workers is already a well-entrenched policy. More than half of the respondents say they regularly employ on-call hourly part-time workers. And 84% to 90% use independent contractors and make regular use of temporary workers, either hired directly or supplied by agencies.

HIRING MORE AND MORE CONTINGENT WORKERS

▲ PERCENT OF 93 MAJOR COMPANIES SURVEYED
DATA: CONFERENCE BOARD

Further, such use is growing rapidly (chart). Within five years, no fewer than 35% of multinationals expect contingent workers to make up at least a tenth of their workforce—a trend fostered both by the need for labor force flexibility to meet demand fluctuations and by head-count restrictions imposed on managers in an era of continued downsizing.

Still, there's some question as to how widespread this trend really is. According to a household survey conducted by the Bureau of Labor Statistics in early 1995, only 6 million people, or about 4.9% of the workforce, are contingent workers. That's using the agency's widest definition, which counts all workers who expect their jobs to end within the next year or two.

The BLS also reports that about 10% of workers are now employed under what it terms "alternative arrangements"—including independent contractors and freelancers, on-call workers and day laborers, and workers for temporary-help agencies and contract firms. But it notes that not all such workers meet its definition of contingent.

Many experts feel the BLS definition is too narrow. For example, some would count the 4.4 million part-timers whose current jobs aren't in jeopardy but who would prefer full-time work.

What's indisputable is that workers themselves are far from happy about the growing trend toward contingent employment. Two-thirds of contingent workers interviewed by the BLS said they would rather have regular, permanent jobs. Those who didn't mind the arrangement were mainly students.

...AND JAPAN JOINS THE CLUB

Female part-timers are the key

Contingent work arrangements are on the upswing in Japan also. In a recent article in the *Monthly Labor Review*, economists Susan Houseman and Machiko Osawa report that part-time employment there jumped more than 80% between 1982 and 1992 and now accounts for more than 16% of the nation's workforce. And temporary workers, mainly those hired directly by companies on short-term contracts, compose another 11.5% of workers.

Tax breaks have bolstered the trend. Most part-time and temporary workers in Japan are married women, and secondary household earners who make less than $13,000 or so a year don't have to pay income taxes on their earnings. At the same time, Japanese employers don't generally have to pay unemployment, pension, and health insurance taxes for part-timers and temps.

Greater use of part-timers and temporary workers allows Japanese business to gain flexibility and hold down labor costs at a time of unprecedented economic pressure. It also helps explain the continuing survival of such traditional employment practices as lifetime job security and promotion based on seniority for regular "core" workers.

MORE COSTLY GOLDEN YEARS

Retiree medical plans get rerigg

It's a safe bet that future retirees be paying higher fees for Medic What many may not realize, howeve the extent to which their private hea care bills may be rising as well.

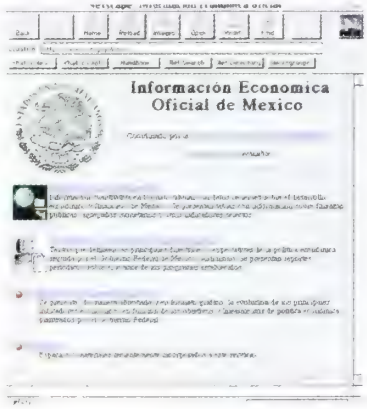
Since an accounting-rule change 1993 forced employers to recognize ture costs of retiree health insura reports consultancy William M. Me Inc., large companies have manage cut projected costs per employee b hefty 29%—mainly by gradually incr ing retirees' contributions, deductib and co-insurance payments. Some ployers have also capped their fut costs or tightened eligibility requ ments. And a few have simply scra their retiree health plans entirely.

THE PESO MEETS POINT AND CLICK

Mexico's vital signs hit the Web

A year ago, as Mexico's economy s out of control, investors and ec mists scrambled in vain for timely nomic data, frustrated by the tradit al secretiveness of Mexico's central and government agencies.

No more. Since August, the Mex finance secretariat has offered a sp economic data pag the World Wide (http://www.shcp.go or http://200.4.80 The page provides to-date informatio English and Spa from such source the Bank of M and the National tistical Institute. eign reserve data released each Wed day, and gross do tic product figures slated to appea days after a quarter ends. Also feat are private-sector economic foreca



The Internet page owes its start to the $50 billion economic re package engineered by Washingto March, which made timely informat condition of the deal. From a few ers last August, the number of p logging on weekly has jumped to

By Elisabeth Malkin in Mexico

JAMES C. COOPER & KATHLEEN MADIGAN

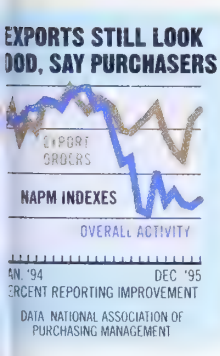
STARTING THE NEW YEAR WITH A BIT OF A HANGOVER

U.S. ECONOMY As New Year's Day often proves, excess can be costly. e same is true for the economy. But instead of suffer- a headache from too much champagne, the economy coping with an inventory hangover due to overpro- ction. It's also hurting from a cooler pace of consumer ending brought on by slower job growth and credit- d bills rung up during the holidays.

These problems continue to box in the nation's indus- al sector. The latest tidbits of economic data—culled m private sources since the government shutdown delayed all official releases—show that the economy ew at a sluggish pace in the fourth quarter. What's re, that softness seems likely to extend right into ly 1996.

Factories scaled back their production in December, t domestic demand was equally soft. So inventories bably remained somewhat excessive, and producers l have to lower output schedules again this quarter. ll, despite worries about consumer debt, the economy ms unlikely to drop into a recession.

OW GROWTH IS THE WORD from the December ort of the National Association of Purchasing Man- ment—the most important data to be released since itdown II began. The NAPM's composite index of in- trial activity rose to 47.3% in December, from 46.5% November, but any reading below 50% suggests t the industrial sector is contracting.

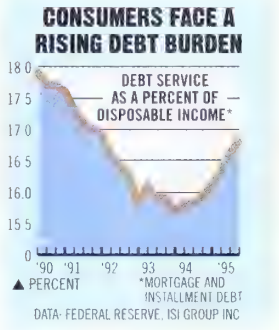


Of the individual components, the NAPM's production index, while up from November, was low enough to suggest that production fell last month. And the more forward-looking new-orders index slipped to 45.9% in December, from 50.1% in November, indicating that factory activity remains in the doldrums.

Factory payrolls still look e under pressure. The NAPM's employment index roved to 47.2%, from 44.1%. It takes a reading ve 47%, over time, to suggest that factory payrolls rising. And because the Labor Dept.'s employment ase scheduled for Jan. 5 has been indefinitely de- d, the NAPM report is the best available sign that, at very least, manufacturing jobs were flat last month. ne bright spot in the economy remains the foreign or. The NAPM's export index rose to 57.4% in December—the highest reading since July (chart). Strong foreign orders reflect better growth prospects overseas, especially in emerging markets. Given the global technology boom, it is not surprising that the NAPM reveals that industrial and commercial equipment and computers as well as electronic gear were key industries reporting increased export demand.

Factory inventories declined in December, but at a slower rate than in November. And there was another telltale sign that the gifts under the tree last year weren't the usual Christmas largesse: The NAPM indicates that inventory gains were largest in the miscellaneous category, which includes items such as jewelry, toys, sporting goods, and musical instruments.

With slowing demand and high inventories, companies were able to fill orders quickly. The supplier delivery index stood at 48.3% in December. That's above November's 45.8%, but any reading below 50% indicates delivery times are short.



The imbalance between sales and goods-on-hand also means that pricing power continues to wane. The index of prices paid slipped to just 40.8% in December. That's the lowest reading in 4½ years, and just half the index's level in the first quarter of 1995.

The NAPM data echo the weakness seen in other recent private-sector reports. The American Production & Inventory Control Society's manufacturing index slipped in December, and the Association for Manufacturing Technology says that orders for machine tools dropped in November. And according to the *Johnson Redbook Report*, retail sales at department and discount stores for the entire month of December finished 0.6% below their November level.

THE WEAK READINGS on production, price pressures, and retailing heighten expectations that the Federal Reserve will cut short-term rates again at its next policy meeting on Jan. 30-31. The Fed trimmed its federal funds rate on Dec. 19 by a quarter-point, but the malaise setting in now suggests another slice, especially if a credible deal to cut the deficit emerges.

Lower rates could diminish one consumer worry for 1996—high debt levels (chart). But even five years of growth have not made job security a sure thing. These

two factors are likely to limit the gains in consumer spending but not trigger a tailspin into recession.

The Jan. 2 announcement of 40,000 layoffs made by AT&T highlights the precarious position of workers. The surprisingly large and involuntary job cuts may shake consumer confidence in the economy in January.

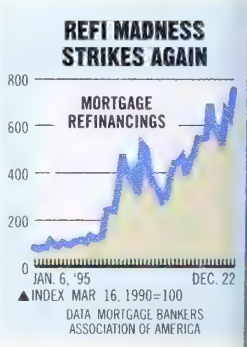
IN ADDITION, CONSUMERS now face their biggest debt burden in nearly four years. Installment debt has increased by $225 billion in the past two years, and home mortgages are up by nearly $300 billion.

Even with the decline in interest rates in 1995, the cost of paying off these two types of debt had risen to 16.8% of disposable income by the third quarter, up from 15.9% a year ago. Given the continued increase in credit-card use, debt service probably rose further in the fourth quarter. Credit-card and mortgage delinquencies are also on the increase.

However, this debt burden is still below the level that signals trouble. For one thing, delinquencies are limited to a small percentage of households. Also, the bond-market rally and the December easing by the Federal Reserve will offer some relief in coming months. Finance charges may slip a bit because so many credit-cards have adjustable rates that are tied to the prime, which banks trimmed by a quarter-point—to 8.5%—right after the Fed cut.

Equally important is the cash-flow boom to homeowners who are refinancing in the wake of the bon market rally. Thanks to 30-year mortgage rates slippi below 7%, refi madness is reigniting. To be sure, th wave does not equal the 1993 gold rush, yet. But the end of 1995, the value of refinancings was alrea seven times bigger than in the first quarter of t year, according to the Mortgage Bankers Assn. (char

Refinancing a $100,000 mortgage from, say, 8.5% to the current 7% can free up $105 in the monthly budget. Moreover, if long rates continue to slip—and right now it seems as if only a failed budget agreement will short-circuit market sentiment—then even more mortgages will be refinanced. That will mean extra money to keep consumer spending on a slow but steady upward trend.



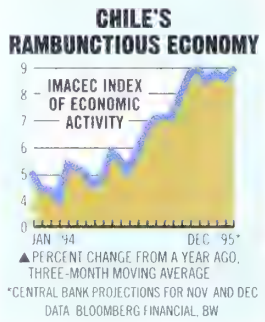
The budget agreement, however, remains a big " on the economic landscape. Until Washington's numb crunchers get back to work, policymakers and priva economists must examine all data shards to see how t expansion is doing. Right now, the private reports su gest that the economy is slowing. Perhaps soon will have some government data to confirm or de that view.

CHILE

MORE SMOOTH SAILING IN SANTIAGO

Chile is an anomaly in Latin America. Unlike in Mexico or Argentina, policymakers aren't grappling with recession, a weak currency, or a dearth of foreign capital. It's just the opposite.

Chile's economic fundamentals are solid: a 25% saving rate, excellent external finances, an expected eighth straight budget surplus, and a strong dollar-pegged peso. Chile's economy appears to have grown more than 8% in 1995, with inflation continuing to trend downward, hitting a 35-year low of 8.2%.



Officials were worried that growth, led by a 15% advance in domestic demand, would be too fast to assure another year of declining inflation. That concern prompted the central bank to lift benchmark interest rates by a full point, to 6.7%, in early December. Chile has also issued new curbs to further limit the inflow of short-term "hot money" into its already tightly regulated financial markets. So analysts expect economic growth to cool a bit in 1996 to about 7%, with inflation slowing to a similar pace.

If policymakers can pull off a soft landing, Chilean equities should show another good year. They were something of a regional haven in 1995 amid uncertainty over Latin America. Also, analysts expect robust domestic demand in '96 to fuel 20%-to-30% growth in corporate earnings.

One downside of such vibrant demand, combined with last year 5%-to-6% appreciation of the pes is more imports. Chile's trade bal ance went into deficit at midyear although the full year should pos a surplus. That surplus may slip this year, especially amid weaker prices for copper, which accounts for a third of Chile's exports. Sti Chile holds a generous $14.5 billion in foreign reserves.

In an effort to further enhance its trade prospects, Chile is work ing to gain entry into the North American Free Trade Agreemen and the Mercosur trade groups. Temporarily stymied in those efforts, officials announced on Dec. 29 that they will negotiate their own trade agreement with Cana da. Chile already has a separate pact with Mexico.

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TAX POLICY

JACK KEMP

FLAT-O GAMBL

The flat tax is key to the GOP's '96 agenda. Politically, it's a tough sell

Mired in the actuarial agonies of budget-cutting, Republicans are about to revive the pro-growth optimism that was a hallmark of party idol Ronald Reagan. On Jan. 9, a commission led by former Housing Secretary Jack F. Kemp, an apostle of supply-side economics, is expected to endorse a flat income tax that promises to promote both growth and investment.

The commission will place the Republican Party squarely behind a radical overhaul of the tax code. Indeed, the GOP hopes that tax reform, with its accompanying IRS-bashing and pro-growth rhetoric, will form the centerpiece of its 1996 campaign. But the Kemp panel also will trigger a ferocious debate. The combatants: Democrats committed to preserving tax progressivity and curbing corporate welfare vs. Republicans bent on applying a one-size-fits-all rate to all paychecks, whether earned by a secretary or a corporate tycoon.

The panel draws its clout from its sponsors. The brainchild of Senate Majority Leader Bob Dole (R-Kan.), the group is composed of 14 members selected by Dole and House Speaker Newt Gingrich (R-Ga.). It also has a big push from the rise of GOP V House contender Malcolm S. Forb The publisher has ridden his advoca a 17% flat-tax proposal—backed b estimated $20 million in advertisin a surprising No. 2 spot in Iowa New Hampshire polls.

Kemp's report will offer Republi three guiding principles for refor will call for a single rate on earne come, an end to the double taxati corporate profits and dividends, a new congressional requirement th ture hikes in the tax rate rece "supermajority"—a vote by 60 more of both houses of Congres pass. For multinationals and expo the panel also might suggest tha Treasury tax only U.S. income

TING RETURNS: *The GOP figures it exploit resentment of the IRS*

s, wiping out a rat's nest of regula-
s on taxing foreign-source income.
he report is silent about just what
new flat-tax rate should be, and it
s the politically charged issue of
ther Americans would have to give
wo of their cherished write-offs: de-
ions for home-mortgage interest and
itable contributions. Left on his
Kemp would have provided many
ie key details. But Dole, the GOP
idential front-runner, urged Kemp
ick to generalities to deny oppo-
s an inviting target. Grouses a Sen-
GOP aide: "If you stick in a rate,
lebate quickly becomes 'What's your
t?' and 'Who's going to pay more?' "

Flat Tax: The Proposal...

The Kemp Commission's probable recommendations:

FLAT RATE A single tax rate will apply to all income, with generous personal exemptions for low-income taxpayers.

ONE TAX Reform would end double taxation of business income by exempting either savings or capital income from tax.

SUPERMAJORITIES Congress would have to muster 60% or greater majorities to raise the tax rate.

...And The Reality

Key issues still unresolved:

HOW MUCH? The commission won't propose a specific rate. And while taxing interest and dividends at the corporate rate makes economic sense, it will look like a windfall for the rich.

NO DEDUCTIONS? A pure flat tax would wipe out all deductions. But Kemp will leave the door open to keeping popular breaks for mortgage interest and charities, at the price of a higher rate.

CAN THE GOP AGREE? Supply-siders are willing to shrink government to get a lower tax rate—but Republican leaders want revenue-neutral reform. And Kemp's report won't settle the arguments between flat-taxers and those favoring a national sales tax.

DATA: BUSINESS WEEK

Instead, Kemp will lean heavily on attacks on the current tax system, indicting its complexity, its waste, and the befuddled incompetence often displayed by the Internal Revenue Service. "Our No. 1 goal is to make sure that everyone knows that the tax system we've got now is broken," says S. Jackson Faris, president of the National Federation of Independent Business and a member of Kemp's panel.

That will draw cheers on the radio-talk circuit, where GOP activists have been beating the tax-overhaul drums for two years. "There really is a strong feeling across the country that the time has come to start over with a new tax code," says Kemp panelist Shirley D. Peterson, a former IRS commissioner and now president of Hood College.

Not all Republicans share Kemp's enthusiasm for the flat-tax fix. House Way & Means Committee Chairman Bill Archer (R-Tex.) will push his own national sales tax alternative, despite the lukewarm reception it got from the Kemp panel. Other Republicans worry that the flat tax is vulnerable to attacks by President Clinton as another GOP giveaway to rich investors.

Indeed, the White House can draw ammunition from dissenting GOP economists, who calculate that some flat-tax proposals will boost levies by 25% for working-class families. "If you're watching your neighbor pay less tax because he's getting most of his income from interest and dividends, the flat tax doesn't look so great," warns GOP strategist William Kristol. The flat tax "is not the magic bullet Republicans thought it would be."

TOUGH SELL. To win over the public, GOP reformers will have to make the case that the current system overtaxes capital income. In accounting terms, that's a no-brainer: Corporate profits are taxed at the corporate level, then again when they're paid to individuals as dividends or capital gains. "We've got to eliminate the bias against savings in the current code," says Kemp panelist Carroll A. Campbell Jr., president of the American Council of Life Insurance.

But easing that double burden, as GOP flat-tax or sales-tax plans propose, will give big breaks to savers and investors at the expense of wage-earners. Politically, that's a tough sell. The middle-class whammy could be doubled if the flat tax eliminates all itemized deductions. The 17% flat tax backed by House Majority Leader Richard K. Armey (R-Tex.), like Forbes's, gets rid of write-offs for mortgage interest, state and local taxes, and charitable gifts.

Although only 27% of taxpayers actually claim such breaks, GOP pollsters warn that flat-tax support plunges when surveys explain that reform may eliminate deductions. Taxpayers "are very parochial in what they want to protect," says Republican pollster Anthony Fabrizio. Kemp's report will try to put the best face on the touchy issue: It won't recommend which deductions to keep, but will note the tradeoff between keeping deductions and cutting the tax rate. Armey would have to raise his flat-tax rate from 17% to 20% to retain the mortgage-interest deduction without losing revenue.

Flat-tax activists, delighted by the backing of the GOP's top leaders, are certain that their plans can overcome any doubts about fairness to the middle-

class. "We're finally bringing the debate to Washington—the only city in America where the flat tax isn't popular," exults Grover G. Norquist, president of Americans for Tax Reform, a grassroots lobbying group. Congress' tax-writing committees will launch hearings on overhaul in the spring—provided, of course, that the battle over balancing the federal budget is finally cleared away.

The real battleground, though, will be out on the hustings. For GOP candidates running against Washington, there's no juicier target than the IRS. And those with a supply-side bent can trumpet the pro-growth potential of a simpler tax system with flat rates and fewer loopholes. Republicans hope that a 1996 sweep of Congress and the White House will give them a clear mandate to overhaul the federal tax code in 19

Perhaps. But if Republicans plan march behind the banner of a pure tax, they'll have to ask the middle-cl to ignore their calculators, overlook th doubts, and vote against their pock books. That's a tall order—and it ma the flat tax a huge gamble for the G

By Mike McNamee and Howard Gle man, with Lee Walczak, in Washingt

THE BUDGET

NOW THE ONLY THING CERTAIN IS DEATH

Figuring taxes will be a crapshoot until the stalemate is over

As if paying Uncle Sam weren't enough of a headache. This tax season, things may be even uglier than usual. The reason? Without a federal budget deal that would have finalized tax rules for 1995, some taxpayers still don't have a rule book to follow in their filings. That could lead to widespread confusion for taxpayers, problems for tax software providers, and a more-hectic-than-usual season for the nation's tax preparers. "If there are a lot of changes [in the final budget deal], we'll have a lot of hiccups," says Marion Mason, a certified public accountant in Miami.

One reason for the uncertainty: A slew of tax breaks for both corporations and individuals expired in 1995 and have yet to be renewed. While Congress is expected to restore most of these breaks in its final budget agreement, including a tax exemption for tuition assistance and a research tax credit for corporations, the delay could cause major accounting headaches. Meanwhile, early filers could be forced to hold off until a deal is reached—or risk having to amend their filings.

IN THE DARK. For individuals, the answers to unresolved questions could make a big difference in their tax bills. The Republican budget plan calls for a new, $500-per-dependent tax credit for children and a cut in the capital-gains tax to 19.8% from the current 28%. As now written, both provisions are retroactive to taxpayers' 1995 returns. The trouble is, the Internal Revenue Service tax forms now being mailed out across the U.S. don't include these proposed alterations.

As the debate drags on, it becomes less likely such changes will be made retroactive, most tax experts say. Still, the possibility exists: Capital-gains tax forms now include a warning from the IRS that Congress could make changes to the 1995 rules. And if the stalemate lingers into February, taxpayers still hoping for a cut in the 1995 capital-gains rate will be left hanging. Judy Keisling, a vice-president with H&R Block Inc., is advising clients who want to do their taxes early to use the current capital-gains rate. If the stalemate lasts much longer, she warns, the uncertainty could even begin to disrupt personal tax planning for 1996.

> A slew of tax breaks for companies and individuals expired in 1995. Some may not be renewed. Even those that are may be revised. Accountants are bracing for a major migraine

The nation's corporate filers are as much in the dark about the final look of their tax bill for future years. President Clinton, for instance, has proposed taxing 50% of the dividends corporations earn on stock investments, instead of the current 30%. A change for 1996 would substantially impact the investment retu companies can expect. Although it is clear whether that provision and oth like it will actually be altered, Washi ton conventional wisdom says that s tax breaks will ultimately be elimina or reduced. Corporate clients "are v concerned about this," says Deloitt Touche tax principal Clint Stretch.

PREPARING FOR THE WORST. Equ unnerving for business is the fate such popular provisions as the ex sion of employer tuition assistance f an employee's taxable income. Autho for the provision expired on Dec. 1994. While the exclusion is exped to be extended, at least for r the provision is technic no longer in effect.

Accountants are b ing for major headac as a result. The forms that many ployers are now g erating reflect hig taxable income for ployees who received ition assistance du 1995. If the provisions restored, employers will h to reconfigure those forms. " could cause people to have to amended returns later," Rachelle B. Bernstein, a par with Arthur Andersen & Co.

Most tax software compa are betting that Washing won't make any major cha to the 1995 regulations. they're preparing for the w Intuit Inc., which will begin s ping the final version of its Turbo software in late January, will m changes available to users through World Wide Web page or by ma them an updated program. TaxCu program from Block Financial Softw a unit of H&R Block, is also prep to mail maintenance disks and will fixes to user forums available on o services. Inconvenient? Yes. Expen too. But whoever expected balan the budget to be any fun?

By Amy Barrett, with Dean Fous Washington, and bureau reports

COMMENTARY

By Dean Foust

THE RTC'S EPITAPH: IT WORKED

Even for the U.S. government, it was a colossal undertaking: In 1989, Uncle Sam created the Resolution Trust Corp. to dispose of the assets of hundreds of failed savings and loans. The RTC quickly became the nation's largest financial institution, eclipsing even Citibank.

From the start, RTC officials faced enormous skepticism. Critics charged that RTC sales tactics, aimed at unloading assets as quickly as possible, were enriching wealthy investors while undermining local real estate markets. And persistent whiffs of scandal—from Price Waterhouse billing the government $25 million for photocopying at one San Diego thrift to charges that then acting RTC chief Roger C. Altman gave the White House an improper "heads up" on the agency's probe of Whitewater—only fed the perception that the RTC was spinning out of control.

But now that the RTC has closed its doors for good—on Dec. 31, a year ahead of schedule—it should be commended. Despite federal rules that hindered its negotiating flexibility and a civil-service pay scale that made talented managers hard to recruit, the RTC transformed itself into a Washington rarity: a federal agency that worked. The RTC did a pretty good job, given that they were expected to be entrepreneurial—which is hard for most government agencies to do," says Bert Ely, an Alexandria (Va.) financial consultant.

OLD HANDS. The RTC mostly was run by experienced business executives such as former American Airlines chairman Albert Casey. Management, in turn, signed over 100,000 contracts with real estate professionals who managed properties, held auctions, and packaged assets to be sold on Wall Street as securities.

The bottom line: Of the $456 billion in assets that it inherited, the agency recouped $395 billion, an impressive 86% return. As a result, the thrift cleanup, including the expense of running the agency, should cost taxpayers about $145 billion—far less than the most dire forecasts. Having disposed of a jumble of 747 ailing S&Ls—25% of the industry—the government has left a legacy of 1,460 remaining institutions, 90% of them operating in the black. What's more, the RTC's rapid sales helped establish a floor for the moribund real estate market and dispelled a cloud that could have weighed down the economy for a decade.

Not that the thrift liquidation agency still hasn't much to answer for. It presided over one of the largest wealth transfers the nation has ever seen. The RTC's insistence on bundling some assets into pools so big that only the largest Wall Street firms could bid severely limited the pool of potential buyers and allowed early takers to reap annual returns of up to 40%.

However, other nations, especially Japan, could learn much from the RTC. Japanese leaders are still trying to contend with an estimated $800 billion in worthless assets on their banks' books. They plan to develop an RTC-like institution to dispose of failed housing-loan corporations, but they have been loath to do the same for troubled banks—a big reason why that economy remains so weak.

The U.S. thrift crisis was painful, all right, but better policies emerged from the suffering. Banks and thrifts now must meet higher capital standards. And a 1991 law forces regulators to act as soon as an institution's tangible equity falls below 2% of its assets. In addition, a year-old law restricts maximum payments to depositors in failed institutions to the $100,000 insurance limit, thereby imposing some market discipline.

Washington still hasn't learned all the right lessons. Regulators have yet to find a way to keep banks from placing big bets on interest rates. Dozens of banks got stung by rising rates as recently as 1994. But on Dec. 12, a group of federal examiners pulled back on a plan to require greater disclosure of interest-rate risk at banks by March.

Today, though, there's probably little risk of surging rates flattening banks anytime soon. And all things considered, the U.S. economy looks strong for the moment—in no small part thanks to the RTC's success. Chalk it up as one case where government bureaucrats really did what they set out to do—and then turned out the lights.

Foust covers economic policy from Washington.

CLEANING UP A CRISIS

MARCH, 1980

Congress lifts the ceiling on the rates that savings and loans and other banks can pay for deposits, enabling S&Ls to become go-go speculators.

SEPTEMBER, 1983

Would-be financier Charles Keating acquires Lincoln Savings & Loan.

MARCH, 1985

Government shuts Florida securities dealer ESM, triggering run on Ohio thrifts.

APRIL, 1989

Government seizes Lincoln Savings & Loan from Keating, declaring it insolvent. Taxpayer cost: $2 billion.

AUGUST, 1989

Congress creates Resolution Trust Corp. to oversee sell-off of thrift assets, with William Seidman as first head.

DECEMBER, 1990

Resolution Trust Corp. holds its first auction. All told, the agency holds hundreds of local auctions as well as eight national ones and sells billions in assets from failed thrifts such as Centrust.

DECEMBER, 1995

RTC shuts down for good. Final thrift cleanup cost to taxpayers: $145 billion.

AT&T IN NYC: *Ass writedowns and consolidation wil cost over $3 billio*

DOWNSIZINGS

THE BLOODLETTING AT AT&T IS JUST THE BEGINNING

The telecom industry may ax 100,000 more jobs over five years

It is perhaps the driest, most arcane piece of legislation Congress has ever devised, and its path through Washington has been agonizingly slow. The landmark bill that would reform the telecommunications business might not even pass until late January, a year after it was introduced. Already, though, it is setting into motion a top-to-bottom industry restructuring that will require years of wrenching change.

The pain began in earnest on Jan. 2, with AT&T's announcement that it will eliminate 40,000 jobs, 13% of its workforce, over the next three years. The cuts will be one of the biggest job reductions in corporate history and the largest ever in the telecom industry. And for the industry overall, they won't be the last: While AT&T Chairman Robert E. Allen lamented the "difficult and painful" job cuts, he added: "I believe the reductions and other actions are absolutely essential if our businesses are to be competitive."

Such is the fallout from legislation that many members of Congress promote as a "jobs creation" bill. The legislation, nearing completion in a joint congressional committee, will give local phone companies, long-distance carriers, and cable-TV operators entry into each other's businesses for the first time, unleashing a wave of creative and competitive forces. Along the way, some 3.6 million new jobs will be created, according to a Baby Bell-sponsored study by consultant WEFA Group.

First, though, the longtime monopolies and oligopolies that dominate telecommunications will have to learn to live without the regulations and costly barriers to entry that have protected their markets—and without the associated corporate bloat. Beyond deregulation, the fiber optics, wireless telephony, and compression software that vastly multiply the capacity of a phone line means that tens of thousands more calls can be transmitted over a single wire, cutting both the manpower and the money needed to run a phone company. So cable operators, electric utilities, and even railroads can afford to get into the telecom game—and they are.

As a result, says Mark R. Bruneau, president of Boston-based consultant COBA-M. I. D. Inc., some 100,000 traditional telecommuni tions jobs will eliminated in the ne five years, atop t 250,000 cut since t Bell system break in 1984. "I can't thi of any company th has all of their structuring acco plished or is faci the market in exac the way they wa to," says Dwight Allen, director telecom consulting Deloitte & Touc "Everyone is going have to constan adapt and adjust."

"FIERCE." In the p two years, the nation's phone compan have announced plans to lay off so 130,000 phone workers. AT&T has b the most aggressive, shrinking its wo force by 73,000 since 1984, despite the quisitions of NCR Corp. and McCaw C lular Communications Inc. (chart). latest round, though, will cut particula deep—"a good indication that AT&T is ing to be a fierce competitor," says Li B. Meltzer, an analyst at UBS Securi Inc. Most analysts had predicted t only 20,000 to 30,000 jobs would be el inated following the company's nouncement on Sept. 20 that it will br into three separate companies.

AT&T will take a $6 billion write-of its 1995 fourth quarter, including billion to cover asset writedowns the closing, sale, or consolidation of cilities. The charge will reduce 1 earnings by $4 billion, but analysts pect higher future profits that AT&T plow into its next big venture: the lo calling business. AT&T has made it cl that it plans to go after the Baby B as soon as deregulation allows.

The big question, says Merrill Ly & Co. analyst Daniel Reingold, is: "H will they get into local service, and h much will it cost?" AT&T must forge rect links to homes and offices by bu ing its own local networks or buyi major cable operator or competit access provider. But either appro could cost some $5 billion or more, quiring all the efficiencies AT&T muster. The preparations will be pai indeed—and they aren't nearly ove

By Catherine Arnst in New

HAT DARING OLD COMPANY ND ITS JAUNTY JALOPY

rysler bets on Prowler as a cheap way to pep up Plymouth

hey were flights of fancy, a fleet of visionary vehicles dreamed up by employees. But one sketch at ysler Corp.'s 1991 "idea fair" caught eye of design guru Thomas C. Gale. was a hot rod with the flowing forms the early 1930s," recalls Gale. "I dn't wait to build a scale model." ive years later, Gale can't remember who produced that early drawing—

NICHE WHEELS: *There's nothing on the street quite like Prowler*

the notion has become a ng leap for Chrysler. On 3, the auto maker an- nced plans to produce Prowler, a $35,000 retro-styled road- expected to jump-start the stalled ge of its Plymouth brand and serve test bed for future models.

RTHWHILE GAMBLE." For a relatively y investment of $75 million, Chrysler rning out the flashiest niche vehicle e its Dodge Viper muscle car hit pavement in 1992. Prowler will be first U.S.-made production car with ll-aluminum frame and body struc- . And by coaxing suppliers into do- much of the engineering research, ysler not only kept its costs down cemented vendor relationships al- y regarded as the industry's best. he Prowler reinforces Chrysler's tation as far and away the nim- , most inventive member of the Three. With the early blessings of rman Robert J. Eaton and Presi- Robert A. Lutz, the new car flew through design and development. Rivals Ford Motor Co. and General Motors Corp., still bogged in bureaucracy, "couldn't do it for $75 million," says Christopher W. Cedergren, an analyst with AutoPacific Group Inc. "For that price, it's a worthwhile gamble to put some new life into a brand that's been dying for the last 20 years."

The question: Will a $35,000 two-seat convertible set the right tone for a brand that makes its money pitching entry-level Voyager minivans and Neon subcompacts to the middle class? Former Chrysler Chief Financial Officer Jerome B. York, now an aide to hostile Chrysler investor Kirk Kerkorian, calls the vehicle, aimed at affluent car enthusiasts, a "questionable" addition to Chrysler's lineup.

Chrysler execs, though, contend that the Plymouth brand desperately needs some excitement. Less than 300,000 Plymouths were sold last year, compared with nearly 750,000 at the brand's peak in 1973. Research shows that Plymouth has little identity among the first-time car buyers it covets. "There is clearly no real passion associated with the brand," says Steven Bruyn, Plymouth's marketing manager. "Prowler is meant to startle you."

The low-slung, sinister-looking roadster certainly turned heads when it was unveiled as a concept car in 1993. But its limited market meant Chrysler had to keep its own investment modest. The project would fly only if it borrowed heavily from existing parts, if its technology could be extended to mass-market cars, and if suppliers shouldered much of the R&D.

DIMPLES, TOO. No problem. Vendors jumped at the chance to work on Prowler. While few are likely to make money, most envision marketing tie-ins and the prospect of bigger Chrysler orders to come. "Chrysler is the pacesetter—they take risks," says Richard A. Schultz, director of automotive products for Aluminum Co. of America. Alcoa provided 100 frame and body parts for the Prowler; similar parts may go in the next-generation Chrysler LH sedans.

Loading the car with aluminum posed challenges. Body panels had to be riveted rather than welded, and steel fasteners needed special coatings to prevent corrosion. Because aluminum is one-third the weight and stiffness of steel, engineers could only estimate the thickness needed for safety. The frame on one early Prowler was so stiff the car "almost broke the barrier" in a 30-mph front-impact test, recalls Chrysler engineer Craig R. Love.

To add flexibility, Chrysler and Alcoa indented the frame with "dimples" so it would buckle safely on impact. Other suppliers went the extra mile, too. With no room for a spare, for example, Goodyear Tire & Rubber Co. developed oversize tires that can be driven even when flat. And about 40% of Prowler's parts came from other Chrysler vehicles. The result is a stunner. Chrysler may sell only a few thousand Prowlers a year, starting next spring. But in inventiveness, the auto maker will lap the competition again.

By Bill Vlasic in Detroit

A STAR IN THE MAKING

BARGAIN COST Development costs totaled just $75 million, cheap by Motown standards.

ENGINEERING SMARTS Some 40% of the Prowler's parts are borrowed from other Chrysler cars. Aluminum is 30% of its overall weight.

SUPPLIER SYNERGY Chrysler required vendors—even direct rivals—to work as a team. Suppliers absorbed a big chunk of engineering and tooling costs.

MARKETING BANG Prowler will be key to reshaping Plymouth's stodgy image. The hot rod enhances Chrysler's reputation as the boldest of the Big Three in design.

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SCANDALS

GOLDINGER—HE'S NOT THE MAN WITH THE MIDAS TOUCH

The SEC is probing trading practices at Capital Insight

He's normally quick to answer questions from the press about investing and markets, but these days, S. Jay Goldinger isn't returning calls. Following the December disclosures of massive investment losses at two of his biggest clients, Goldinger effectively shut down operations at Capital Insight Brokerage Inc. and has instructed his staff to refer all inquiries to his lawyers.

At the heart of the firm's downfall seems to be a mistaken bet that interest rates would rise in late 1995. When rates instead declined, Goldinger faced big losses in the Treasury futures contracts he had bought for clients through Refco Group Ltd., a Chicago clearinghouse. So far, two companies have declared losses that Goldinger's lawyer confirms derive from investments with Capital Insight: Retailer Pier 1 Imports Inc. announced on Dec. 26 that it had lost $20 million, and manufacturer PairGain Technologies Inc. revealed on Dec. 1 that its account was $16 million in the red.

AMAZEMENT. Losses on futures are nothing new. But at least one of these companies claims its funds were to have been invested in low-risk instruments. That Goldinger could find himself in his current position amazes many who believed in the public persona he had created. "I was shocked," says Brien Lundin, president of Jefferson Financial, the corporate host of a New Orleans investment conference Goldinger regularly addressed. "He's one of the last people I would have imagined being involved in risky investments."

For years, Goldinger assiduously polished his public image, getting himself quoted regularly and making high-profile charitable donations. He became a financial-advice columnist in 1988, when he offered his services to Charley Blaine, business editor of *The Times-Picayune* in New Orleans. Blaine had him write a weekly piece that Goldinger eventually syndicated to several other papers. "He's a fairly hyperactive guy who liked to keep his name in the public eye," says Blaine, who canceled the relationship after Pier 1's loss became public. Goldinger's visibility fed on itself. Lundin says he was an especially popular speaker at New Orleans conferences because of his syndicated columns.

Goldinger began his investing career in 1977 at Cantor Fitzgerald LP. He left in January, 1988, to start Capital Insight with three colleagues. The new firm thrived despite a Securities & Exchang Commission probe into insider tradi while Goldinger was at Cantor. Accordi to the SEC, Goldinger gave inside info mation about the pending takeover Thrifty Corp. to Capital Insight founder Bert R. Cohen, who traded on for his own account and others'. La May, a California district court dismiss the charges, but the SEC is appealin Another problem: Capital Insight ma aged to lose $10 million for a client, T ton Group, between 1989 and 1990.

PIER 1 ACCOUNTS. Still, by 1993, Capit Insight was managing cash accounts Pier 1 and PairGain as well as investi for as many as 43 other clients—includi top executives of Pier 1 and PairGain.

For PairGain, things went fine un late 1994, according to Robert A. Ho a director. Hoff will not name Capi Insight as PairGain's adviser but sa that's when the company explicit asked its adviser simply to b and hold ultrasafe Treasuries a stop trading in futures and tions. In June, 1995, manageme asked that the accounts be liq dated—and that's when troub hit. The accounts took fi months to clear, and PairGa was finally told it had lost million of its $28 million cash count. Goldinger's lawyer, Br O'Neill, did not return calls a ing for comment on Hoff's piction of events. Refco's lawy assert that Goldinger had discretion over the accounts a that regular statements w sent to all of his clients.

PairGain is considering legal tion: It has hired Deloitte Touche to investigate the los and a law firm to advise outs board members on their optio Pier 1 executives will not c ment on Capital Insight, tho Director Sally F. McKenzie s the board was "comple shocked and horrified" by the l es, which it learned about on 22. O'Neill didn't return calls ing about McKenzie's stateme

Meanwhile, the SEC and C modity Futures Trading C mission are investigating—q questing trading data and ot documents from investors Refco. Goldinger may be sit now, but eventually he'll hav explain why he pursued a st egy that lost a mint.

By Nanette Byrnes in Angeles, with Stephanie An son Forest in Dallas

HIGH VISIBILITY Goldinger very carefully polished his public image, becoming a popular speaker and financial columnist

A CHECKERED CAREER

1977 Jay Goldinger joins the Beverly Hills office of investment firm Cantor Fitzgerald.

1986 According to the SEC, Goldinger gives inside information on the upcoming sale of Thrifty Corp. to colleague Bert Cohen, who trades on the tip.

1988 Cantor Fitzgerald closes its West Coast retail operations; Goldinger, Cohen, and two other Cantor alums found Capital Insight Brokerage.

1988 Goldinger begins writing a financial-advice column for New Orleans' *Times-Picayune*; eventually, he syndicates the column.

1989–90 Capital Insight loses $10 million of the Triton Group's account betting on interest rates.

1993 Capital Insight begins managing the cash account of PairGain Technologies.

1995 PairGain and Pier 1 announce losses totaling $36 million from Capital Insight. Regulators begin an investigation. Capital Insight effectively closes.

DATA: BUSINESS WEEK

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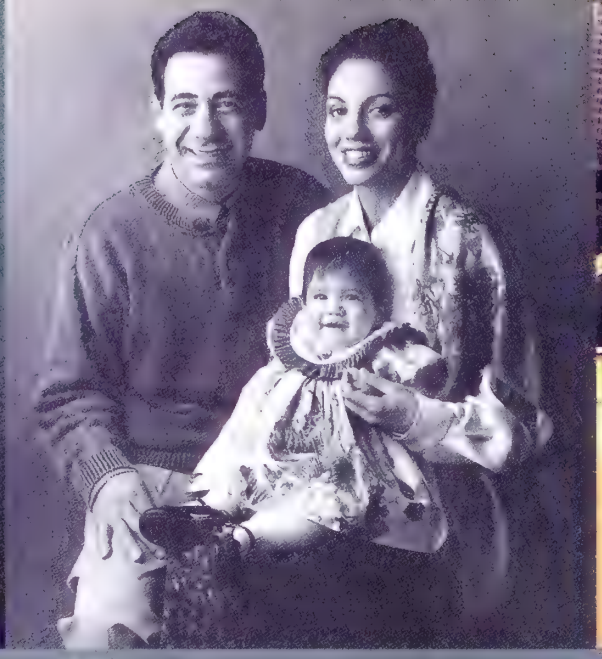
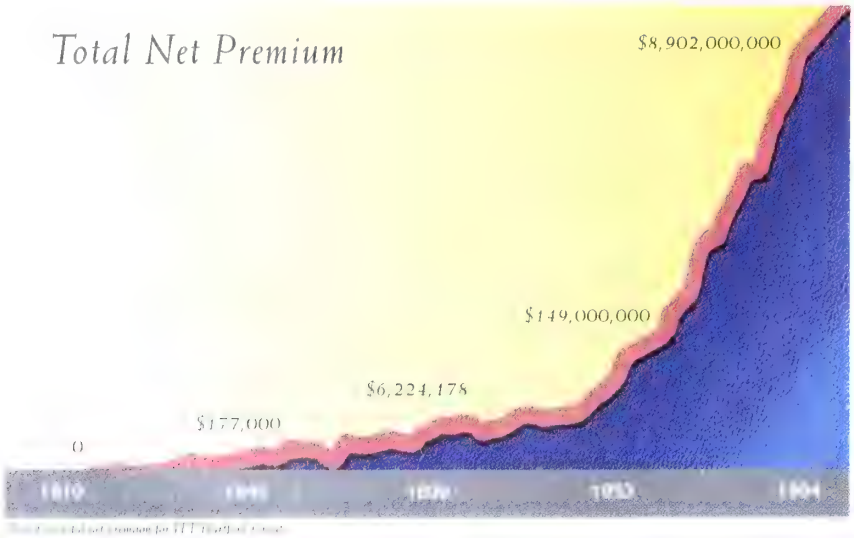


WHEN you SPEND as MUCH TIME W

your SHAREHOLDERS, an I



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ITT HARTFORD

COMPUTERS

BABES IN CYBERLAND

Can Compaq turn the PC into a plaything for tots?

With Christmas toys still cluttering bedrooms and dens, it hardly seems the time to be cooking up new ways to dazzle kids. But that's what personal computer kingpin Compaq Computer Corp. and preschool-toy giant Fisher-Price Inc. have in mind. On Jan. 4, the two planned to announce a line of new compu-toys that could turn the home PC into 1996's toy story.

The immediate goal of this big-name combo: Get the 18 million U.S. families with kids under age 7 to drop $150 each for computer attachments such as oversize keyboards and car-like controls that make a PC as accessible to the average 3-year-old as a jungle gym.

Long term, Compaq and Fisher-Price aim to keep moms and dads adding on to their investment. The companies are planning a stream of $40 adventure and learning programs that work with the companies' add-on keyboards and toy controls. "We hope to create a myriad of products and software that last for a long, long time," says Fisher-Price Chief Executive Byron Davis.

CHILD-SEAT DRIVERS. Analysts estimate that developing the new products could cost upwards of $15 million—before marketing costs. But if Compaq and Fisher-Price succeed, they will have helped redefine the home PC as much more than a home office machine. The compu-toys also may give Compaq a way to eclipse rival Packard Bell Electronics Inc. next year in home PC sales (chart). Compaq Chief Executive Eckhard Pfeiffer has pledged to make the company twice the size of its nearest rival by the end of the decade. To get there, though, Compaq must keep entering hot markets.

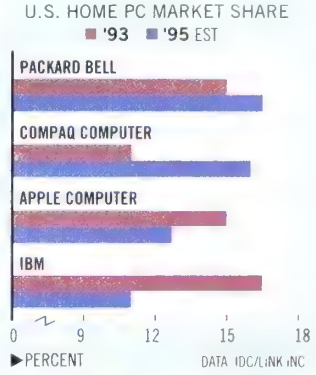
The first fruits of the Fisher-Price collaboration take aim at electronic educational aids and "edutainment" software. The $150 Wonder Tools Cruiser is a driving toy that lets a child use a throttle, steering wheel, and horn to navigate adventure programs such as *Spruce Squirrel's Hiccup Mix-Up*. The second attachment, a $130 keyboard, is geared to children's small hands. The add-ons, says Compaq Consumer Vice-President Celeste Dunn, couple existing PC learning programs with toys. "We're excited," says Toys 'R' Us Inc. Chief Executive Michael Goldstein, who plans to carry them beginning this summer. Adds Compaq's Dunn: "We expect this to be a significant sector of growth for us."

PLUGGED IN

Fisher-Price and Compaq are teaming up on the Wonder Tools Cruiser. Price: $150

HOUSE-TO-HOUSE COMBAT

U.S. HOME PC MARKET SHARE



It would be a surprise if it were Shipments of electronic learning to are growing at about 28% a year a were expected to hit $290 million 1995, according to the Toy Manufact ers Assn. Sales of educational and r erence software grew by 142% la year, to $600 million, according to searcher IDC/Link Inc. And softwa publishers such as Davidson & Asso ates Inc. rake in profit margins of 7 to 80% on titles such as Davidso *Ready For School.*

PERIPHERAL VISION? Compaq isn't alo in its pursuit of the kiddie market. Jan. 5, Packard Bell is due to launch families group, dubbed Packard Bell teractive. Toy retailers say IBM and crosoft Corp. also are developing so ware and hardware releases this ye

And game mak such as Sega Ent prises Ltd. are tering the mark Sega's Pico comp er, which attaches a TV, already s well during 1995.

Together, thou Compaq and Fish Price believe th can stay ahead of the competition. C paq is recruiting multimedia devel ers to build software for Wonder To planning 14 titles this year and aim to release new ones every six mon thereafter.

Not everyone believes the com toys will prove to be winners. "It's e to be determined whether consum will purchase software that requ the additional cost and installa of peripherals," says a Davidson spo woman. Compaq says the software on standard PCs, and the add-on simply make the programs m fun and interactive.

However this s ends, the Fisher-P tykes are one of eral audiences Compaq is likely chase through sin partnerships, Richard Zwetch baum, PC analyst a ternational Data C "What it's doing for 3- to 7-year- can be extende teenagers, to wor single moms, to th niors market," he Let the games be

By Gary Williams in Ho

GAG RULES: *Protesting pending telecom reform in San Francisco*

E INTERNET

LT.SEX.BONDAGE IS CLOSED. HOULD WE BE SCARED?

e Net is fast becoming a global free-speech battleground

ondage. Blondes. Bestiality. Even Barney. (Don't ask.) Subscribers to CompuServe Inc. could indulge all e passions and more—until Dec. 28. n, without warning, the online ser- provider cut off access to more 1 200 such forums and picture data- es distributed over the Internet. iography was not computing.

was a defining moment in cyber- e, where information providers and ributors are hurtling toward a series nfrontations that could reshape their lectual, moral, and commercial bound- s. As millions of people around the e plug into the Internet and com- cial online services, many govern- ts—unnerved by the prospect of un- rolled, grass-roots communications— readying their regulatory guns.

H POINT. That much became clear the CompuServe incident. The pany acted after a German state ecutor's office said is breaking the law llowing access to pornography. Al- gh its customers can get to the ed forums by dial- irectly into the In- et, the decision ked a furor among speech advocates n the online com- ty. "It really does you down a slip- slope," says Esther Dyson, chairman of the Electronic Frontier Foundation, a political action group. "Now it's indecency; when does it become political speech?"

More international tangles are taking shape. In China, where the number of Internet users jumped from 3,000 to 100,000 last year, the government is cracking down on "spiritual pollution" in the form of pornography and anti-government material entering the country via the Internet. Data-line licenses in Jordan bar service providers from "indecent" content. And telecommunications-reform legislation in the U.S. includes a provision that would make it a criminal offense to transmit material deemed indecent over the Net.

Pornography is the first flash point in an inevitable clash of cultures forced by the borderless Internet. There is no easy way to tailor Net content for a particular country or geographic area—as CompuServe found when it was forced to shut off access to all subscribers to satisfy German law. As a result, many Net proponents fear that the lowest common denominator will prevail. "Differences in community standards—whether state to state or country to country—pose a real threat that freedom of expression will get nibbled down to nothing," says David D. Redell, an executive committee member of Computer Professionals for Social Responsibility in Palo Alto, Calif.

WATCHING CONGRESS. Still to come: a Pandora's box of multinational issues involving taxation, intellectual property, and privacy. For example, government policies on data encryption vary widely, hampering the development of a worldwide standard that would spur electronic commerce and, ironically, keep adult content such as pornography out of sight of minors. How governments respond to these challenges could determine the Net's commercial viability. Censorship would "take what could be a major business and a major opportunity and stunt its growth," says David J. Farber, a professor of telecommunications at the University of Pennsylvania and an Internet pioneer.

Not all countries will follow Germany's example. "I do not foresee any censorship on porn," says Joy Marino, president of the Italian Internet Assn. Many Net denizens favor technological alternatives to censorship: Already, a number of software programs let parents filter what children can access. In any case, many governmental solutions will be frustrated by the Internet's sheer breadth. Attempts by the United Arab Emirates and Bahrain to create electronic barriers to certain Internet sites have proved leaky.

For now, many countries are watching to see whether the U.S. Congress' actions will stand up. Experts predict that any legislation prohibiting transmission of "indecent material" will go to the courts, where it will be found unconstitutional. That may not stop countries with weaker free-speech protections from trying to control the Internet. But they're not likely to succeed: Online communication is hard to track and harder still to stop.

By Amy Cortese in New York, with John Carey in Washington, David Woodruff in Bonn, and bureau reports

CENSORING CYBERSPACE *Government efforts to legally impede the spread of "indecent" content on the Internet*

U.S. An amendment to telecom-reform legislation would make it a crime to knowingly transmit "indecent" materials over the Net. Punishment: $100,000 and two years in jail.

GERMANY Lawmakers are clamping down on online-service providers that allow access to child pornography, which violates German criminal law.

CHINA The government is planning to introduce new regulations to restrict the flow of "pornographic and detrimental" information into the country via the Internet.

MICHAEL MACIOCIA/JEAN-LUC LAGARDE

In Business This Week

EDITED BY KEITH H. HAMMONDS

JUICING UP WESTINGHOUSE

CHAIRMAN MICHAEL JORDAN of Westinghouse Electric is hurrying to drive up the company's long-suffering stock—and keep media-hungry raiders at bay. As 1996 began, he put in a poison-pill provision to raise the cost of taking over Westinghouse and its newly acquired CBS. Two days later, he announced the $3 billion sale of the company's defense-and-electronics division to Northrup Grumman. Jordan has raised $4.2 billion from asset sales. Now, he expects to pay down 65% of the debt he took on to buy CBS last fall. Equally important, Jordan's pitch that Westinghouse is undervalued seems to be finding believers. Following the Northrup announcement, Westinghouse shares rose 7.3%, to a 12-month high of 18¾.

CHRYSLER: HOW BIG A BUYBACK?

JEROME YORK PUT ON A GREAT show. In a speech in Detroit on Jan. 2, Chrysler's former CFO—now point man for billionaire shareholder Kirk Kerkorian—suggested that Chrysler could afford to buy back $2 billion in stock a year. The crowd ate it up—but missed the best part: York said later in an interview that Chrysler could spend up to $9 billion on buybacks through 1998. Chrysler Chairman Robert Eaton's response: "I don't think Jerry York knows what he's talking about." But York sensed a different reaction from investors. "They didn't exactly throw tomatoes, did they?" he quips.

A TAX BREAK IN THE SKY

THE BUDGET IMPASSE IN Washington may have ruined the holidays for hundreds of thousands of federal workers, but it brought cheer to air travelers. The 10% federal excise ticket tax, which expired on Dec. 31, hasn't been reauthorized by Congress. So some carriers, among them American Airlines and Delta Air Lines, have reduced ticket prices 10% since Jan. 1. Washington probably won't try to collect the tax retroactively, says one House aide—unless the impasse drags on for several more weeks. The government stands to lose $13 million a day.

RITE AID'S SQUEEZE PLAY ON MEDCO

MANAGED HEALTH CARE LOST a big battle in Maryland. After Rite Aid and several other big drugstore chains refused to fill prescriptions for government employees, the state was forced to cancel a new $266 million contract with Merck's Medco Containment Services. It was a big win for Rite Aid CEO Martin Grass, who has waged a two-year court battle against drugmakers for alleged discriminatory pricing. Rite Aid has several similar "situations" pending in other states, says an executive. But Maryland's Attorney General may investigate whether Grass and other drug chain chiefs illegally conspired to shut Medco out.

RELAX. MICKEY IS FINE

MESSY STRIKES IN FRANCE'S public sector have ended, but the workers at Disneyland Paris have caught the protest wave. Several dozen of them fought with the park guards on Dec. 31, after they h been refused entry to de onstrate for higher p When the melee cleared, employees were slightly i jured—Mickey not amo them. Workers at the Fren park had been appropriat cheerful in recent years, lowing earlier prote against rules concerning dr and facial hair. Now, Fren business leaders hope the rest isn't a sign of strike ver spreading to the priv sector.

ET CETERA . . .

■ Carson Pirie Scott en its bid for Younkers, wh will merge with Proffitt's

■ International Paper exe tive Mark Suwyn will get top job at Louisiana-Paci

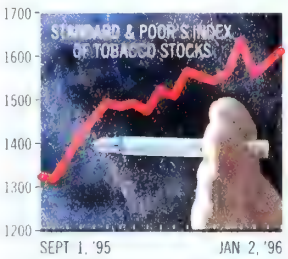
■ Umang Gupta will re from the struggling softwr company he founded.

■ Aston Martin, once Jam Bond's car of choice, come to the U.S. with the DB7 Vola

CLOSING BELL

SMOKIN'

Even for tobacco, the past few months have been tough. The Food & Drug Administration is trying to regulate cigarettes as a drug and cut off minors' access, and second-hand-smoke lawsuits are advancing. Still, tobacco stocks are up 25% since midsummer: International sales are robust, and more young people are lighting up again. Plus, experts think the industry's 12-volume argument challenging the FDA's regulatory effort will delay action that could cost the industry more than $1 billion a year.



DATA: BLOOMBERG FINANCIAL MARKETS

HEADLINER: DAN DORFMAN

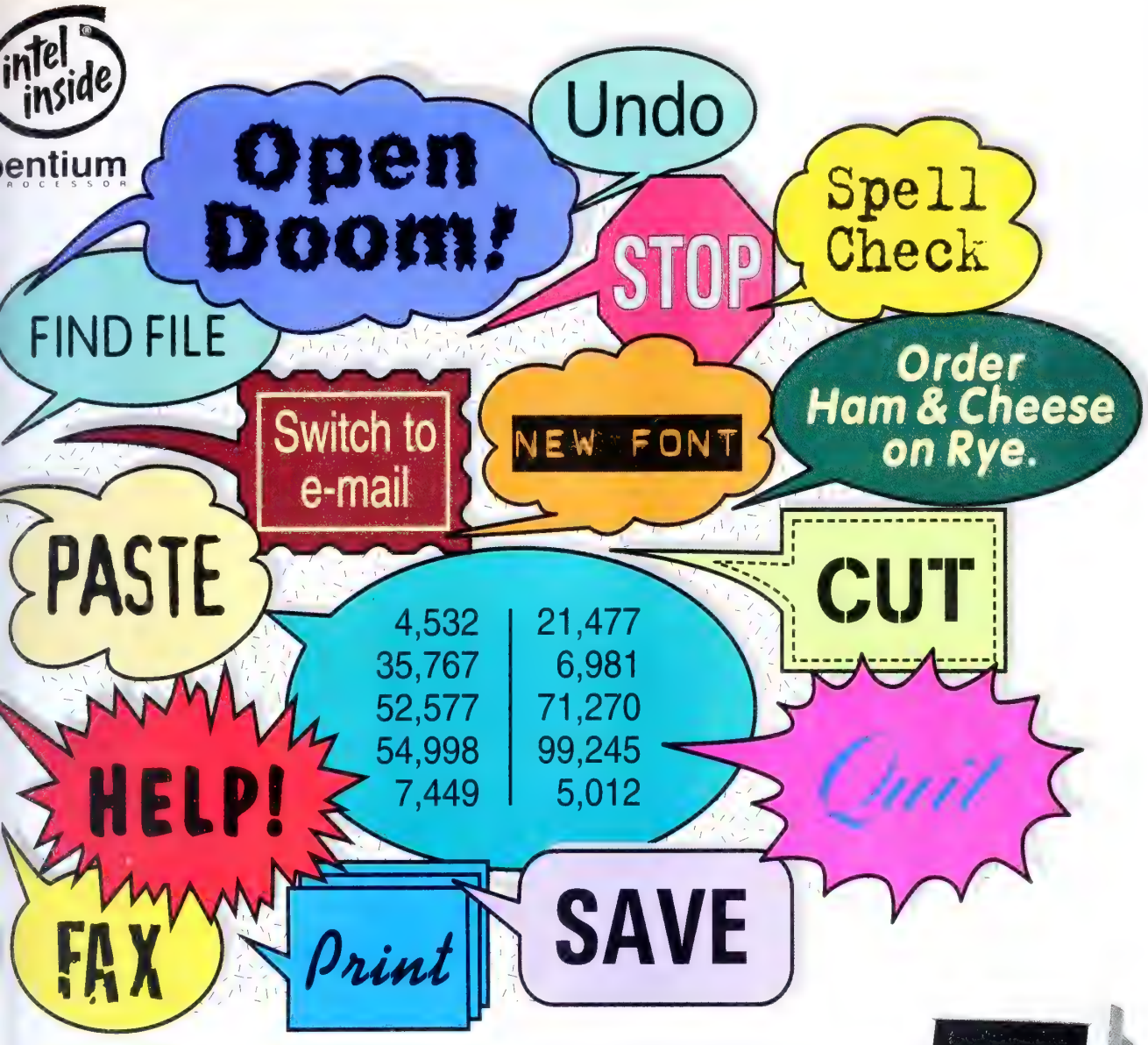
LOSING *MONEY*

The new year got off to a rocky start for Dan Dorfman, the TV and magazine stock tipster. On Jan. 1, *Money* magazine fired its columnist for refusing to disclose to his editor the sources he uses in reporting his columns.

Dorfman had been on paid leave from the magazine since BUSINESS WEEK revealed in October that Dorfman and stock promoter Donald Kessler were being investigated by the U. S. Attorney's Office in Brooklyn for possible securities-law violations and wire and mail fraud. *Money* Managing Editor Frank Lalli says he asked for Dorfman's sources "to maintain my confidence in the quality of the information we publish." In a statement, Dorfman said he couldn't comply with *Money*'s "sweeping demands."

Estimates pu Dorfman's income at more than $1 million a year from speaking fees and salaries from CNBC television and *Money*. CNBC has continued to air Dorfman's daily stock reports, and a spokesman said that the network still sees "no reason to believe that Dorfman has violated the law."

By Michael Schroede



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DITED BY OWEN ULLMANN

FOR NOW, CLINTON HAS A CONTRACT WITH BLACK AMERICA

s President Clinton and Capitol Hill Republicans haggle over a balanced-budget deal that will slash Great Society programs, a sense of abandonment is growing in Black nerica. After all, African Americans would bear a dispro-rtionate burden from cutbacks in subsidized medical care, using assistance, job training, and dozens of other govern-nt benefits. Yet Bill Clinton's political standing with black ers is not going the way of the disappearing welfare state. Why? Newtophobia. While many African Americans are appointed that Clinton hasn't been a stronger advocate for eral social programs, House Speaker Newt Gingrich (R-Ga.) s become so loathsome to blacks that s generating a rally-'round-the-Presi-nt movement, despite Clinton's right-rd tilt. A December Harris poll, for mple, found that only 15% of blacks proved of Gingrich's performance.

NDING FIRM. Civil rights activist Jesse kson says that Gingrich has stirred up black community "just like Bull Con-' and George Wallace did. He's mean-rited and he has a radical disregard the neediest people." Three months , Jackson flirted with an independent sidential run that could have wrecked Clinton's prospects. now, Jackson appears to have shelved his own candidacy ocus on electing Democrats in '96.

Clinton has also helped his cause by fighting Gingrich & Co. r a few issues of transcendent importance to black Amer-ns. He refused to reverse his support for affirmative-action cies, held out for more Head Start funds, and drew a bud-ary line in the sand over summarily ending Medicaid. esident Clinton walks the walk when it comes to domestic cy," says Detroit Mayor Dennis W. Archer, a Democrat. ther moves have cemented Clinton's hold on black voters. was careful to endorse the "personal responsibility" theme he Million Man March while distancing himself from or-ganizer Louis Farrakhan. And he has stood by two embattled African American Cabinet officers: Commerce Secretary Ronald H. Brown and Energy Secretary Hazel R. O'Leary, despite GOP calls to fire them.

Ron Lester, president of polling firm Lester & Associates, notes that Clinton's positive rating among blacks has jumped in his surveys from 63% a year ago to 80%—higher even than ratings for Jackson or Colin L. Powell. "We feel comfortable with Clinton," says Lester, who is black.

The President's campaign strategists want to maintain that comfort level through Election Day. They believe a heavy African American turnout is essential for Clinton to carry crucial swing states such as California, Illinois, Michigan, New Jersey, and Pennsylvania. For starters, the President plans to deliver a major address on Martin Luther King Day as a reminder of his commitment to the black community. And his campaign is planning get-out-the-vote drives to reverse 1994's sharp drop in black turnout. Jackson has pledged to help register 8 million new voters. "This generation can defeat Gingrich and his forces," he says.

JACKSON: *Giving Democrats a hand*

Still, other black leaders want to keep the pressure on Clinton to ensure that he doesn't move rightward again. Grumbles Northeastern Illinois University political scientist Robert Starks: "Clinton will go whichever way the wind blows." One idea is to present Clinton and the GOP nominee with an African American contract adopted at a national convention this summer. Says Howard University political scientist Ronald W. Walters: "We have to exercise some leverage."

If Clinton takes their support for granted, disaffected black leaders are talking of boycotting the race. But with Gingrich vowing to make a new run on the welfare state, opinion in Black America is crystallizing—in Clinton's direction.

By Richard S. Dunham

CAPITAL WRAPUP

TUCK AT THE SEC?

Securities & Exchange Commission-Steven M. H. Wallman's hopes to re-ace Mary Schapiro as chairman of the mmodity Futures Trading Commis-n got a boost on Jan. 2. The Senate firmed Utah lawyer Norman S. nson to an SEC seat. Joining Wall-n and Chairman Arthur Levitt Jr., nson raises to three the number of nmissioners on the five-member nel. Rules allow the SEC to conduct siness with only two commissioners, ting Wallman move to the CFTC even as the Senate reviews the nomination of University of Akron law professor Isaac C. Hunt for another SEC seat.

A CLOSE EYE ON TRADE

▶ President Clinton's trade hawks will strike a tough pose this year. The Commerce Dept. and U. S. Trade Representative are setting up offices to make sure foreign nations live up to trade accords with the U. S. Insiders say campaign politics is behind the effort: Breast-beating against trade scofflaws appeals to rising economic nationalism among voters.

BORK: THE RACERS' EDGE

▶ Reagan Supreme Court nominee Robert H. Bork is burning up legal rubber for some race-car drivers. On Dec. 28, Bork filed objections to proposed Food & Drug Administration rules to restrict cigarette advertising at sports events. Bork, who represents such drivers as Mario Andretti, Al Unser, and Rusty Wallace, asserts that the rule violates the First Amendment right to free speech. At stake: big bucks. Winston alone spends $40 million a year sponsoring races.

CHINA

A CHILL WIND BLOWS FROM BEIJING

To keep control, its leaders are cooling risky reforms

SLOW TRACK: *The government wants more wealth to go to poorer provinces such as Sichuan, where a miner carts co*

Hu Angang, an economist at the Chinese Academy of Sciences, is one of the government's favorite intellectuals. His is a distinctly conservative voice. Educated at Yale University, Hu, 42, promotes policies intended to preserve social stability in China rather than achieve rapid economic reforms. For instance, to spread wealth to poor interior regions, Hu wants to end privileges for special economic zones on the coast once favored by Deng Xiaoping.

With the ailing Deng, 91, increasingly out of the picture, Beijing's insecure leaders are heeding the words of people such as Hu who argue that China can't afford the bold moves Deng long advocated. "If a leader of 1.2 billion people makes one little mistake, it could end up being a big danger," Hu says.

That's just one example of the chill winds blowing from Beijing as the country prepares for the Chinese New Year. Intent on preserving their control in the post-Deng era, Communist leaders are retreating from many risky economic policies. That means no major reform of state enterprises or the banking system—long seen as crucial to completing the transformation of China's economic system.

The new mood is spilling over into China's relations with the outside world. As he tries to consolidate power, President Jiang Zemin is hanging tough on such sensitive issues as Taiwan and human rights. Beijing's decision to slap rights activist Wei Jingsheng with a 14-year sentence in December is a reflection of the new hard line.

For Washington, the tough tone has troublesome implications. China had a record trade surplus of nearly $40 billion with the U.S. last year, and the sides are making little progress in solving difficult trade issues. Given imprisonment of Wei, the Clinton ministration will likely increase its forts to have the U.N. Commissio Human Rights censure China in Ma Moreover, China's use of military neuvers to intimidate the Taiwan who vote in their first direct preside elections in March, is likely to ad tensions in Congress.

DEAL KILLERS. American companies have new worries. Now that Vice-P mier Zhu Rongji has engineered a " landing" of China's once-overheated e omy, the government wants to ensu "soft takeoff," economic growth wit the dramatic swings of the Deng d That's good news. But Beijing's p to scrap some preferential tax poli for foreign companies is causing t

think twice about moving ahead with ojects in China. "The changes will kill lot of deals in the New Year," says nne Stevenson-Yang, Beijing director the U.S.-China Business Council.

Although China remains a lucrative arket in sectors such as telecommuni-tions, many companies are concerned th plans to eliminate duty-free status r imported machinery and to abolish x rebates for exports of gh value-added goods. eneral Motors Corp., for ample, which recently se-red a $1 billion deal to oduce sedans in Shanghai, uld be affected unless it ns an exemption. "These nds of tax swings are to expected in an emerging onomy," says GM Chairman hn F. Smith Jr. "You have flow with the changes."

A slowdown in foreign in-stment may not trouble e leadership if it helps to ep inflation under control. ice Zhu launched an aus-ity program in 1993, infla-n and economic growth ve moderated. Growth in 95 slowed to about 10%, m 12.6% a year earlier, ile retail prices eased m a 21.7% rise in 1994 to ound 15% in 1995.

ATHING. One reason for leadership's conservative x of policies is the fear it poor inland provinces falling too far behind. gns of restiveness are erywhere. Workers have en demonstrating over un-d salaries, rising unem-yment, and falling stan-ds of living. In early cember, 500 migrant rkers from the interior shed with police in a ody riot in Guangdong. minimize unrest, Beijing's lers want to recentralize ver. The government, for mple, is beefing up a new tax system ensure that Beijing gets a bigger e of the pie from the richer prov-es, which would allow it to pour more ds into inland areas for infrastruc-e, agriculture, and education.

Provincial leaders in Guangdong and ian provinces are fighting to keep r privileges. The party chief of Shen-n, the special economic zone adja-t to Hong Kong, wrote a scathing cle in the local press attacking the new policy proposals. Guangdong officials also are upset about the central government's decision to cancel tax rebates for value-added exports.

The changing signals in Beijing are disheartening to reformers. "There will be no big push for change," says Hai Wen, deputy director of Beijing University's China Center for Economic Research. Change is especially needed in the state sector, one of the biggest drags on the economy. Since state-owned factories employ some 50% of the urban population, the leadership isn't willing to let them go bust. But they won't let the larger factories privatize, either.

Instead, modest experiments are the rule. Beijing is selecting 1,000 big enterprises to run their own operations free from government interference. The government will also help forgive massive bank loans by allowing them to swap equity for the debt. In 1996, the number of enterprises involved in such experiments may reach 4,000, accounting for 50% of the production value of all state-owned companies.

The best hope for major reform is for China to get into the World Trade Organization. As a member, China would be forced over a designated period of time to liberalize its economy by dropping many trade barriers. But Chinese officials involved with the negotiations aren't hopeful. "Recent negotiations have not made any progress," says Li Zhongzhou, a director general at the Ministry of Foreign Trade & Economic Cooperation. "I'm very pessimistic." While Jiang announced in November that China would lower tariffs on 4,000 products by no less than 30% in 1996, Chinese officials have yet to disclose which goods will be included.

Clinton Administration officials question whether China's leaders seriously want to join the new trade tribunal. They note that Beijing has not fully responded to the "road map" for membership that Washington provided in November. China also has failed to crack down effectively on piracy of U.S. intellectual property. In an election year, rising economic nationalism doesn't give the Administration much wiggle room. "The political reality is that WTO accession will be colored by overall relations," says Charlene Barshefsky, Deputy U.S. Trade Representative.

No one believes China is returning to the era when state planners ruled supreme. But the recentralization is clearly an attempt to enable Beijing to set the pace of economic development rather than cede that power to the coastal provinces. Some analysts even argue that China has outgrown the go-go Deng days and now needs time to consolidate after 15 years of rampant growth. Whatever the case, China's leaders are determined to play it tougher at home and abroad.

By Joyce Barnathan, with Dexter Roberts, in Beijing, Amy Borrus in Washington, and Kathleen Kerwin in Detroit

SIZZLING SHANGHAI: *Foreign business will get fewer breaks*

China in 1996: What to Watch

BALANCE AMONG PROVINCES The leadership is scaling back privileges of rich coastal provinces, trying to shift resources to poor inland regions

ECONOMIC REFORMS Beijing will go slow, further delaying sweeping enterprise changes as well as banking and financial-market reform

ECONOMIC GROWTH Leadership hopes to maintain non-inflationary growth without spurring unemployment

POLITICAL STABILITY Crackdown could intensify on democracy activists and Tibetan followers of the Dalai Lama

FOREIGN INVESTMENT Government could take away special tariff and tax privileges for some foreign investors

FOREIGN RELATIONS Continued conflicts with the U.S. over such issues as Taiwan, human rights, and trade

DATA: BUSINESS WEEK

GERMANY

THE ECONOMY THAT FELL TO EARTH

Germany's slowdown is scaring its neighbors

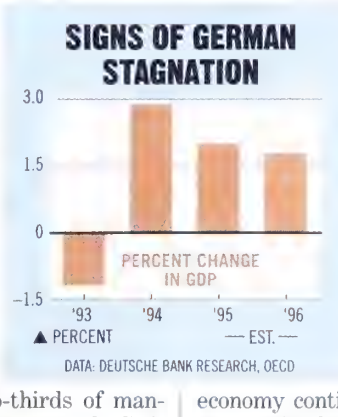
Germany is supposed to be Europe's locomotive. But thanks in part to recent French strikes delaying shipments of German goods, gross domestic product probably will show no growth in the fourth quarter, the second stagnant quarter in a row. Unemployment, rising since last spring, is at 9.3%. Industrial output is 4% below last year's level. And new orders in the engineering industry are plunging. Says Ian Harwood, head of strategy at London's Kleinwort Benson Group PLC: "Fears of a hard landing are growing."

Indeed, while a tax cut, a recent Bundesbank interest-rate reduction, and a widely expected decline in the German mark may produce a brief rebound in the first half, the year ahead looks grim. Unless consumers unzip their pocketbooks in a hurry—and that looks doubtful—Germany will have a hard time even reaching the anemic 2% growth rate it achieved in 1995 (chart).

OUT OF THE WATER. Such downbeat forecasts scare Germany's neighbors. "If Germany slows down, everyone else winds down with it," says Sergio De Nardis, senior economist at Confindustria, the Italian industrialists' federation. That could spell the end of Europe's grand plans for a single currency and monetary union by the start of 1999. European Union nations, led by France, already are struggling to cut budget deficits and cap government debt levels to bring them in line with the Maastricht Treaty. But a serious growth setback starting from Germany would lower tax revenues, raise government borrowing, and bloat deficits across the EU, putting monetary union out of reach and blowing further European unification out of the water.

To a great degree, Germans have themselves to blame for their predicament. Economics Minister Günter Rexrodt attributes the current slowdown to a high mark, big wage hikes, and rising taxes. Add overregulation of business and rigid work rules, and it's no surprise that German companies made $26 billion in direct investments abroad in the first nine months of 1995, double the 1994 rate.

The money is flowing to Eastern Europe, Asia, and even Britain, whose manufacturing costs are 40% lower than Germany's. The huge gap prompted Siemens, for example, to choose Britain as the site for a $1.7 billion semiconductor plant. Consumer-products maker Procter & Gamble Co., meanwhile, has halted new investments in Germany. Its high business costs, warns Harald Einsmann, P&G regional president, risk turning Germany into the "hole in the doughnut" in Europe's industrial landscape.



As manufacturers rethink their commitment to Germany, hollowing out is becoming a growth business. Two-thirds of management consultant McKinsey & Co.'s German trade now consists of helping manufacturers expand production abroad. Says Senior Partner Herbert Henzler: "Germany's present export model—design it, make it, and export it from here—is no longer viable."

With more companies adopting that mantra, workforce cuts will continue. Germany has already lost 1 million j since 1992, mostly in manufacturing. employers' organizations warn that additional 500,000 to 1 million jobs at risk unless wage costs, particul welfare taxes, fall. Little wonder tha one recent poll, two-thirds of east Germans—and half of those in west—told the Allensbach-ba Demoskopie Institut that the risk losing their jobs is their biggest worry.

That's bad news for icymakers who are co ing on a revival of sumer demand. M expect further Bundesb rate cuts, and an $11 lion income tax reduc kicked in on Jan. 1. some analysts wonde the money will find its into stores, noting that ter months of belt-tigh ing to pay higher ta many consumers ar about to loosen up with economy slowing. "We v without so much this that we might consider spending tax rebate]," says Gabi Lewin, a mo of two whose husband works in ar countant's office. "But if things worse over the short term, we m just sock it away and wait."

BEARING FRUIT. Reflecting that cau retail sales fell 2.5% in 1995, the t straight decline, and a hoped-for spurt in Christmas buying failed to terialize. And forget about 1996. poll for the weekly newspaper *Woche* published Jan. 3, 59% of the Germans questi said they expect economy to wor This and other p says Walter Deuss of the Karstadt de ment-store chain, "n point to any dur improvement in sumer confidence."

While Germ waits for consu spending to revive economy continues to flag. If the U any guide, German restructuring ef could start bearing fruit around the the EU plans to get monetary union motion. That could leave Germany competitive than ever. Until then pect anxiety levels to keep rising Germany and across Europe.

By John Templeman in Bonn, bureau reports

EDITED BY STANLEY REED

BRITAIN: AS LABOR SMELLS BLOOD, FOREIGN COMPANIES TREMBLE

Time is running out for John Major. The British Prime Minister wants to postpone national elections until May, 1997, when his five-year term is up. By then he hopes an improving economy will change the minds of voters who now rate him one of the least popular leaders in British history. But the hapless Major may not be able to last that long. Two members of Parliament from his Conservative Party recently deserted. Several others have died in the past year. Major's majority in the 651-seat House of Commons is now down to five votes. February special elections will likely cut it to three. It seems only a matter of time before the harried Prime Minister loses his majority or a confidence vote and is forced to call a snap election that he is almost certain to lose. The Conservatives trail Labor by 30% in opinion polls.

VULNERABLE. At stake is Britain's attractiveness as a low-cost base for American, Asian, and Continental companies. If he becomes Prime Minister, Labor leader Tony Blair is likely to adopt a minimum wage as well as the Maastricht Treaty's costly worker rules. Thousands of foreign companies with some 100 billion in direct investments in Britain are watching closely. So are the 14 other European Union states, because a Labor government is likely to favor tighter ties with Europe.

Major's precarious position leaves him vulnerable to special interests. For instance, he increasingly needs the votes of nine Protestant Ulster Unionist MPs. But their leaders recently warned that their support cannot be taken for granted. That means the Northern Ireland peace talks are likely to be held hostage to Unionist demands.

Seeing Major totter, Labor's Blair is closing in for the lockout. He misses no chance to issue sound bites about the Tory disarray. "It is difficult to see how [the government] can stumble and stagger on for another 16 months," he says. Another good opportunity should come soon: A damning report is expected from a special investigative panel, following a two-year inquiry into whether Margaret Thatcher's government condoned weapon sales to Iraq during an international embargo and just prior to Saddam Hussein's 1991 invasion of Kuwait. Several key Thatcher aides at the time are still in government. Moreover, local elections in May are almost certain to erode Conservative power even further.

MAJOR: *A razor-thin majority*

BICKERING. Major's own Conservatives are almost as big a problem for their supposed leader as Labor. Almost any issue, no matter how trivial, produces a party fight these days. In late December, for example, a handful of Conservative Euroskeptics sided with Labor to defeat Major on a vote allowing Spanish fishermen to enter British waters. But the matter wasn't considered important enough to trigger a confidence vote.

Fed up with this bickering, Major abruptly quit last July as party leader. He thought an election would flush out troublesome right-wingers and restore his credibility. While he won by a comfortable margin, his efforts to placate the right on crucial social issues, such as restricting immigration and cutting benefits for single parents, alienated some longtime Tories. For instance, Conservative MP Emma Nicholson, a former deputy party chairman, made a big splash on Dec. 29 when she blasted the Tories and switched to the Liberal Democrats.

All this makes Major look more and more like a lame duck while Blair plays the budding statesman, jetting off to Japan and Singapore. Major's hopes for another 15 months are looking increasingly unrealistic.

By Paula Dwyer in London

GLOBAL WRAPUP

GERMAN AMBIVALENCE

Germany's sending troops to Bosnia is being hailed as a significant first step toward assuming a bigger world role. But at the same time, the country's military leaders are beginning to question how well prepared the country will be for future operations of this sort. In the 1996 compulsory draft, the majority of candidates opted for alternative social service on conscientious objector grounds. The German brass doubts that it will be able to keep the Bundeswehr staffed at its current level of 340,000 troops.

SAUDI SHIFT

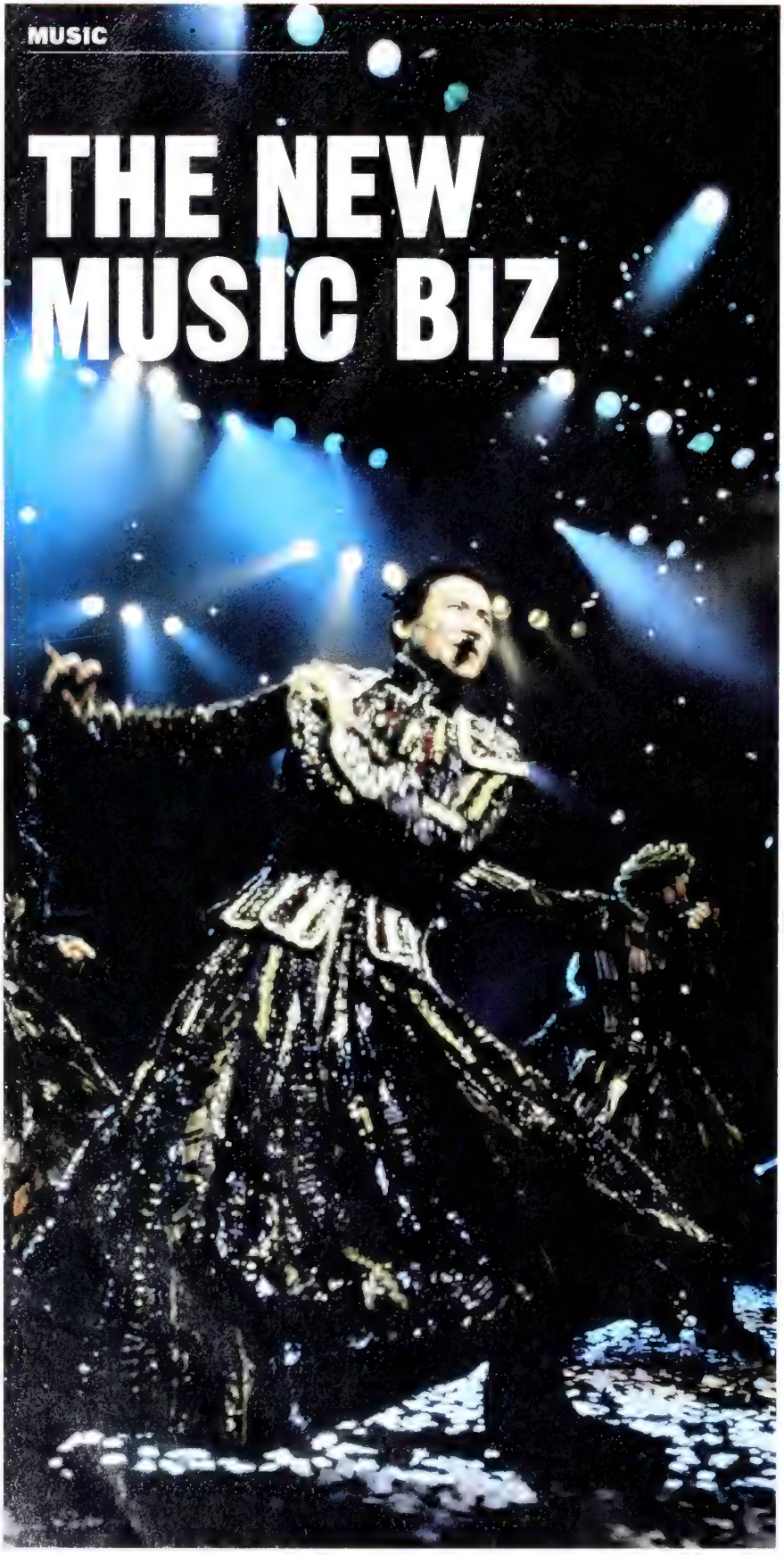
▶ Saudi Crown Prince Abdullah's takeover of the official duties of ailing King Fahd may temporarily cool speculation about royal succession. But it won't put an end to the Saudi problem. There is a natural rivalry between Abdullah, 72, and his supporters and the full brothers of Fahd, including Prince Sultan, the Defense Minister, who is considered second in line for the throne. There are also questions about the suitability of Sultan, 71, who has been the target of withering criticism from Islamic dissidents and others. They say he has used his position to reap enormous profits.

MEXICO'S NEW ENERGY CHIEF

▶ The most important aspect of the recent Cabinet shakeup is the naming of a new Energy Secretary. Jesús Reyes Heroles, a respected economist, is viewed as likely to speed stalled efforts to open up petrochemicals and gas distribution to private investors.

MUSIC

THE NEW MUSIC BIZ



From Beijing to Warsaw, hot local talent is pounding away at U.S. dominance of the music industry

It didn't matter that they we packed into a drafty college dini hall or that they only had a fe hours' notice. They were ready rock. For four hours on a recent Sund night, 3,000 students from the Beiji University of Science & Technolo abandoned their books to enjoy the fo bidden sound of a live concert. Th chanted and waved lighters while s bands—including two of China's hotte stars, He Yong and Dou Wei—blar out Chinese versions of rock, grung and heavy metal.

Because Chinese authorities rare grant permission for rock concerts, tickets were sold. So neither the ban nor the music company that backs the made any money. But the undergrou concert was nonetheless a huge succe The event will help the bands sell hu dreds of tapes and compact disks word of mouth. And that will bolst the reputation of Taiwan's Ro Records, an independent label tha promoting local talent—and taking PolyGram, Sony, and other giants in t region.

HOT SPOTS. Welcome to the new fro tiers of the music business. New Yo and London are on their way out the world's hottest music towns. A the standards for what's hip on the g bal music scene may no longer be det mined primarily by U.S. megastars. day, the action is shifting to spots su as South Africa, where Johannesbur pop-jive sound—a mix of traditional A rican beat, jazz, and rhythm & blues— gaining popularity worldwide. And Hong Kong, where superstar Jac Cheung is creating hits that sell li gangbusters as far away as Amsterda

These days, talent scouts are fanni out to coffee houses in Latin Ameri karaoke clubs Asia, and even sch dances in Cent Europe. They a searching for sing and rock groups w can make it big their own regions catch on around t world. Says K Berry, president EMI Music Inter tional: "The dema

STAR POWER

Hong Kong singer Jacky Cheung is the first Asian artist to make PolyGram's Top 10 roster

· American music is starting to re-
le. Now, the big growth is in local
ists."

The $40 billion music industry is in
e midst of a dramatic transformation.
is changing from a business relying
avily on U.S. sales and exports to
e that is far more decentralized and
ared to local and regional tastes.
ny experts think the U.S. portion
the worldwide music market will
ink to just 20% by 2000, down from
third today and 50% in 1987. After
ars of selling the tunes of Michael
kson and Mariah Carey to overseas
rkets, the five large
npanies that control
% of the industry—
lyGram, Warner,
ny, EMI, and Bertels-
nn—are pouring bil-
ns of dollars into re-
onal studios, plants,
d distribution net-
rks.

Driving the changes
a sales slump in the
S. After a decade of
uble-digit growth,
sic sales in the U.S.
ew by just 2.6% in
e first half of 1995
art). One reason is
e slowdown in com-
ct-disk sales. Over
e last decade, music
es soared as collec-
s converted vinyl
ords and cassette
es to CDs.

Now, that wave is
sting, just as other
blems surface. A
rth of new super-
s has forced compa-
s to dig into their
lts and recycle hits
aging rockers to
st sales. At the same
e, profitability is tak-
a pounding as top
sts with global ap-
l are able to extract
ner fees. EMI paid
million to sign Janet
kson in 1991. Now, the company is
e to signing a new contract for $80
ion to keep her, or she'll bolt to a
peting label. "You have to pay a [top]
e to get a top artist to sign with
" says Rudi Gassner, CEO of Bertels-
n's BMG Entertainment International.
D FAR." Overseas, the picture is far
hter. From Warsaw to Beijing,
ng people in emerging markets are
ding their rising disposable incomes
apes and CDs. And while they will
line up to buy the likes of Bon Jovi
Michael Bolton, they increasingly want to hear stars who speak their own language and reflect their own culture. The lifestyle of, say, Madonna, says an engineering student in Beijing, "is too far from our own." His favorite: Chinese rock singer Dou Wei.

Those preferences pose major challenges for the music giants. With tight government controls and rampant piracy still the rule in many countries, investing in the music business in India or Thailand is fraught with risk. In the old days, exporting Madonna's records and tapes involved little extra overhead cost and even less imagination. Now, music companies must scout out China's emerging pop idols—and struggle with all the cultural, political, and logistical difficulties of starmaking. While local artists make far less than their U.S. counterparts, they can snag $10 million deals if their music sells widely across a region. With recording and video production costs higher in overseas markets, the onus is on companies to find artists with wide appeal.

To make matters worse, the Big Five are facing new competition. Powerful new players such as Seagram Co.'s recently acquired MCA Inc. and DreamWorks SKG are both determined to build a global music business from scratch. Other media giants—Sumner M. Redstone's Viacom Inc., Rupert Murdoch's News Corp., and Michael D. Eisner's Walt Disney Co.—are nosing around the business. One of these companies is expected to pounce on EMI Music when its parent company, Thorn EMI, splits in two later this year.

The Big Five are also battling new regional independents, such as Taiwan's Rock Records, Brazil's Sigla, or Japan's Pony Canyon. Often run by street-wise local entrepreneurs, the independents are savvier about spotting new talent. In 16 years, Rock Records has built itself into eastern Asia's largest independent record company, with 50 Chinese-language artists, including the region's most popular stars. Sales were an estimated $85 million for 1995.

The strains of going global are causing turmoil in the gilded suites of music management. Squabbling over slumping domestic profits and the high price of international expansion are behind some of the tumult. Warner Music Group Inc. is on its third chief in 18 months. Sony's U.S. chief, Michael P. Schulhof, was ousted after poor performance in the company's movie and record businesses.

And while management is stable at PolyGram, weaker-than-expected sales plus delays in new albums forced management to issue a warning that 1995 profits will be flat. "We've all had a good run in the U.S., but it's slowing down," worries BMG's Gassner. "The question is, can we increase revenues in mature markets while we wait for the new ones to develop? It's a very critical time."

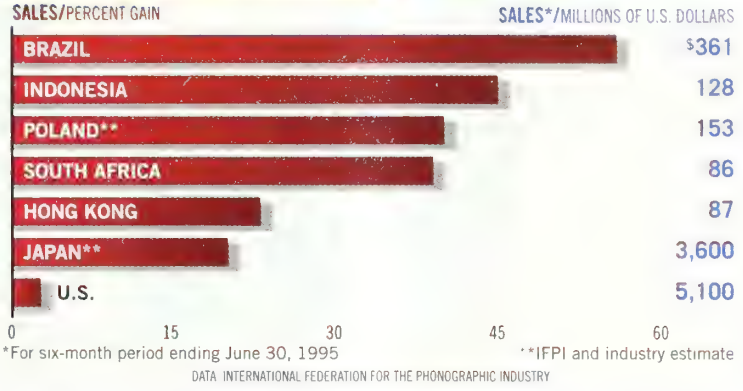
The changing currents initially took

RAPT CROWD

Fans all over the world are like these Taiwanese—they want music and lyrics that speak to their own concerns

Where the Action Is

While the U.S. music market is flat, key foreign markets are taking off



*For six-month period ending June 30, 1995 **IFPI and industry estimate

DATA: INTERNATIONAL FEDERATION FOR THE PHONOGRAPHIC INDUSTRY

many music executives by surprise. Although music companies began to look offshore in the late 1980s, they were mainly selling successful U.S. artists. "Music from the rest of the world was an afterthought," says EMI's Berry.

Then came disappointing sales outside the U.S. Alternative rock bands, such as Warner Music's Green Day and PolyGram's Blues Traveler, haven't been as well received as were Nirvana and Pearl Jam in the early 1990s.

EARSPLITTING. Nor does rap music, so lucrative at home, travel easily. The lyrics conjure up the things Europeans and Asians fear most about the U.S.—crime and violence. French teens are opting for "rai" music, and Italians "ragamuffin," both less harsh Euro-equivalents to rap. Even more popular in Europe is "techno," or dance, music with its earsplitting bass and minimal lyrics. In 1985, U.S. and British artists accounted for 65% of music sales in Europe; now it's just 45%.

Finally, though, the Big Five music companies are starting to catch on to the demand for local music. "Developing local repertoire is our No. 1 goal," says Robert M. Bowlin, president of Sony Music International. He estimates that 80% of the music sold in Latin America is by Latins, while 60% of that sold in Asia is by locals. Says Don Atyeo, general manager of Murdoch's Hong Kong-based Channel [V] satellite music-video channel: "At first, they threw us Stone Temple Pilots and grunge music, which doesn't work here. Now they send us

GLOBAL SOUND

Italy's Laura Pausini has swept Europe, and now, with a Spanish-language record, is a hit in Latin America

80% local repertoire and Western music that works in this market, such as love songs."

Another trend surprises even the most experienced music managers. Known as "the crossover," it's when music from one region outside the U.S. and Britain carves out a big niche in another. Continental European artists are now selling in astounding numbers in Japan, Korea, and Brazil. Warner's Italian chanteuse, Laura Pausini, has swept through Europe and, having recorded a Spanish-language album, is a big hit in Latin America. So is BMG's Italian superstar vocalist, Eros Ramazotti.

Warner's Luis Miguel, Mexico's favorite balladeer, last year sold 500,000 albums in Korea, where he was voted top international artist of the year. EMI's obscure Danish rock band, Michael Learns to Rock, sold 2 million records in Asia, including 500,000 in Japan.

So far, no one has discovered a emerging-market Madonna with worl wide appeal. But Warner Music maest Seymour Stein, who discovered the U. singer, is rolling the dice by promoting mainland Chinese singer called Dadaw worldwide. Warner's Elektra label w release her *Sister Drum* album in t U.S. in mid-January, following a Eur pean tour.

The Shanghai singer, whose re name is Zhu Zheqin, doesn't sound

TAPPING THE GLOBAL MUSIC MARKET

How the Big Five stack up in the race for new sounds

POLYGRAM

WORLDWIDE MARKET SHARE* 19%

SALES**
$4.7 billion

PRETAX OPERATING INCOME
$685 million

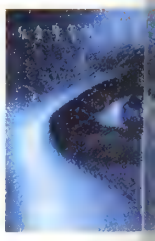
TOP U.S. ARTISTS Bon Jovi, Boyz II Men, Blues Traveler, Stevie Wonder

TOP EMERGING TALENT Ace of Base (Sweden), Jacky Cheung (Hong Kong), MC Solaar (France)

UPSIDE/DOWNSIDE No. 1 worldwide and No. 2 in the U.S., with 13.7% stake. Early focus on building local repertoire now paying off, but top management is distracted by demands of new film unit.

*Estimate **Year ending Dec. 31, 1994

EMI MUSIC



WORLDWIDE MARKET SHARE* 15%

SALES**
$3.35 billion

PRETAX OPERATING INCOME $450 million

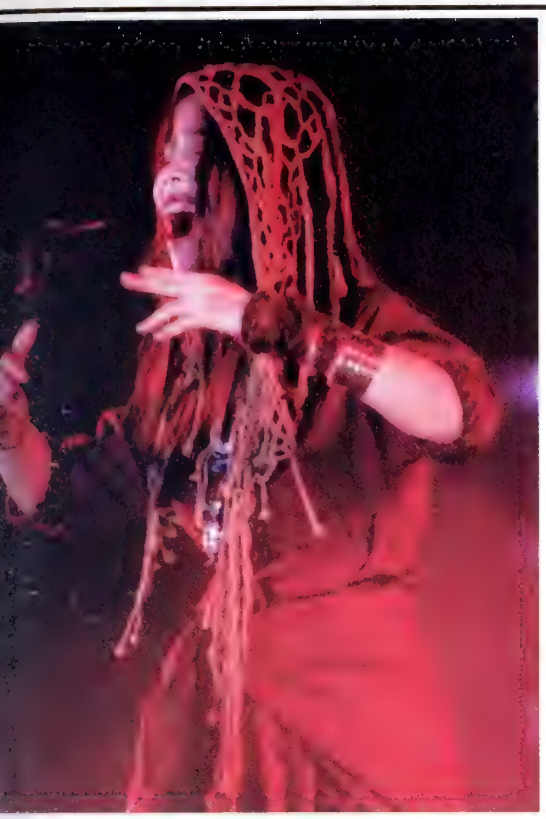
TOP U.S. ARTISTS Garth Brooks, Ed Seger, Frank Sinatra, Janet Ja

TOP EMERGING TALENT Roxette (Sw den), Yumi Matsutoya (Japan) Secada (Cuba), Eric Moo (Taiwa Mamonas Assassinas (Brazil)

UPSIDE/DOWNSIDE Boosted world market share from 10% after b Virgin Records in 1991 and Ja nese affiliate in 1994 but is wa the U.S., with 10.1% stake.

*Estimate **Fiscal year ending Ma

DATA: COMPANY REPORT, SOUNDSCAN, BUSINESS WEEK



t like Madonna, but the two think
ke: She adopted the name Dadawa
cause it's easily pronounced in both
ian and Western languages. Warner's
pe is that the Chinese singer's music,
ich is a mix of Tibetan chants using
ch ancient instruments as the long
mpet, the barreled drum, and the
u fiddle, will resonate with millions of
egorian chant aficionados. Says Bill
edy, president of MTV Networks
ernational: "I think it's only a matter

ASIAN MADONNA?

Dadawa, a mainland Chinese singer about to embark on a European tour, is getting a worldwide push from Warner

of time before a Michael Jackson or a Madonna [emerges] from Russia or Vietnam or India."

South Korea, Taiwan, and Poland, too, are quickly becoming reliable money-spinners, especially now that their governments are reining in illegal sales. Once the greater China market develops—including the 1.4 billion or so Mandarin speakers from mainland China, Taiwan, Indonesia, Singapore, and Malaysia—music companies expect to rack up big profits from investments in Mandarin artists.

And if Mexico and other large Latin American countries can stabilize their economies, the music business could see double-digit earnings growth once again, even without the U. S. Many companies are building a Latin American presence now that Brazil and Mexico are ranked No. 7 and No. 8, respectively, in the world in total retail music sales. PolyGram recently paid $57 million for the region's largest independent, Rodven Records in Caracas.

So far, PolyGram is the market leader. Asia accounts for 25% of its total sales, with such superstars as Jacky Cheung and Faye Wong under contract. Cheung's 1993 album, *Kiss and Goodbye*, sold 4 million copies worldwide, which made him the first Asian artist to get on PolyGram's annual Top 10 roster. "You've got to take your hat off to PolyGram, which was doing 15 years ago what the rest of us are starting to do now," says Michael Smellie, senior vice-president of BMG Entertainment, Asia-Pacific.

ROUGH PATCHES. Now, the others are racing to catch up. "We haven't grown by less than 50% for the past three years, and we expect that to continue," boasts Lachie Rutherford, regional managing director of EMI Music for Southeast Asia and China.

No doubt, there are still rough patches ahead. It will likely take years for government controls to be rolled back and for piracy to be curbed in markets such as China and Russia. But in the meantime, as the new middle class grows in places as farflung as Shanghai, Prague, and Mexico City, music lovers hunger for a mix of local, regional, and American tunes. As the music industry responds, some executives can already hear the sound of money.

By Paula Dwyer in London, with Margaret Dawson in Taipei and Dexter Roberts in Beijing

ARNER MUSIC GROUP

NIDE MAR-
IRE* 18%

lion

OPERATING

million

. ARTISTS Madonna, Green Day, & the Blowfish, R.E.M.

ERGING TALENT Laura Pausini Aaron Kwok (Hong Kong), a (China), Luis Miguel o)

DOWNSIDE Dominates the with 22% market share, but ng catch-up in the global ; building local repertoire

**Year ending Dec. 31, 1994

BERTELSMANN MUSIC GROUP

WORLDWIDE MARKET SHARE* 13%

SALES**
$3.8 billion

PRETAX OPERATING INCOME N/A

TOP U.S. ARTISTS
Whitney Houston, ZZ Top, Toni Braxton, Grateful Dead

TOP EMERGING TALENT Eros Ramazotti (Italy), Masahuru Fukuyama (Japan), So Pro Contrariar (Brazil), Diego Torres (Argentina)

UPSIDE/DOWNSIDE Pushing hard to develop local talent. Weak in the U. S., with 12.2% stake; could see worldwide share slip as distribution agreement with MCA is phased out.

*Estimate **Fiscal year ending June 30, 1995

SONY MUSIC ENTERTAINMENT

WORLDWIDE MARKET SHARE* 17.5%

SALES**
$4.9 billion

PRETAX OPERATING INCOME N/A

TOP U.S. ARTISTS Michael Jackson, Bruce Springsteen, Mariah Carey, Pearl Jam

TOP EMERGING TALENT TUBE (Japan), Harlem Yu (Taiwan), Patricia Kaas (France), Roberto Carlos (Brazil)

UPSIDE/DOWNSIDE Shares No. 2 spot in U.S. with PolyGram; dominates Latin America, but in other markets is overly dependent on American talent.

*Estimate **Fiscal year ending Mar. 31, 1995

SHOP TILL IT DROPS: *Hunting for bargains at a liquidation sale*

RETAILING

EVERYTHING MUST GO—TO THE LIQUIDATORS

Retailing's vultures are getting fat as stores drop like flies

With store chains dropping dead left and right, the past year in retailing has been as dismal as any in recent memory. Except, that is, for the industry's undertakers: the small and all-but-invisible clutch of companies that come in and liquidate leftover merchandise when a retailer shuts down or shrinks. Liquidators purchase the inventory, run the going-out-of-business (GOB) sale, and make a living on the difference. And retailing's plague year has been very good to them: In 1995, they disposed of an estimated $3 billion to $5 billion worth of goods, about double 1994 levels.

Now, as the financial consequences of the latest Christmas bust take hold, another rash of bankruptcy filings is almost certain. "The outlook for the liquidators in the next few years is pretty good, given that we still have several more years of consolidation ahead of us," says Thomas R. Rauh, national director of retail consulting at Ernst & Young.

BIG UNKNOWNS. A handful of major players, all privately held and scattered from New England to the West Coast, may be the biggest retailers no one has ever heard of. Gordon Brothers Partners, a Boston outfit, is operating 800 stores around the country, from Jamesway to Fayva. Schottenstein Professional Asset Management in Columbus, Ohio, will help close 362 outlets of Edison Brothers Stores and 198 of Petrie Stores by the end of the month. Even healthy retailers—or at least viable ones—have started calling in the liquidators to close selected stores as they cut back.

Why don't retailers just hang out their own sales banners and pocket the proceeds? For starters, liquidators pay cash for the inventory—a plus for strapped operators and their creditors—and take on all the risk. "We know what we're going to get going into the deal," says Kevin J. Kulinowski, vice-president for store operations at Jamesway Corp., who expects Gordon Brothers to close the last of the chain's outlets by mid-Januar And for chains that are merely cuttin back, bringing in an outside company t close stores frees management to focu on continuing operations.

Besides, running a GOB sale isn't a easy as just marking down prices. Liqu dators have to have a shrewd eye fo pricing merchandise. And since they tak over operations during a GOB sale, the have to estimate expenses accurately- everything from payroll to phone bil to the big ad budgets needed to lur bargain hunters. A typical sale lasts 6 10 weeks, with markdowns starting 20% and climbing as high as 90% in th final days. Gordon Brothers Presider Robert C. Sager calls his team the Gree Berets of retail. "You drop them in som where, you give them a compass and knife, and they have to survive," he say

INCENTIVES. Indeed, these are not ide selling conditions. To deal with store em ployees who will be out of a job whe the sale ends, liquidators have to craft i centive plans to make it more profitab for staff to stay and work rather tha quit or walk off with armloads of me chandise. Or worse. When W. T. Gra closed two decades ago, employees tri to block the GOB sale by emptying th cash registers. The money went into t bank, but the stores were unable make change. And any miscalculation what the merchandise is worth or ho much traffic ads will generate can be f tal. Says David M. Bernstein, CEO Bernstein Financial Group: "It's like ha ing a party and worrying that nobo shows up." Or too many, for that matt So great was the throng on the fi day of the B. Altman sale in 1989 th Bernstein was forced to close the doo at 3 p.m.

Although the current r tail climate has brought mo opportunity, there's also mo competition. That means liquid tors are paying more to win jo And consumers, who can fi half-price sales any day of t week in their local departme stores, are growing inured screaming GOB sale signs. "GO are losing their touch," sa James L. Schaye, executive vi president of Schottenstein. "Wi have to find something new." may be getting harder to attra mourners, but the funerals wo be stopping any time soon.

By Lori Bongiorno in New Yo

GOING OUT OF BUSINESS

RETAILER	LIQUIDATOR
EDISON BROTHERS (selected stores)	Alco, Nassi Bernstein*, Schottenstein
FAYVA	Gordon Brothers
JAMESWAY	Gordon Brothers
KMART (selected stores)	Buxbaum Ginsberg, Gordon Brothers, Schottenstein
PETRIE STORES (selected stores)	Alco, Nassi Bernstein, Schottenstein
WOODWARD & LOTHROP	Gordon Brothers

*NOW NASSI GROUP AND BERNSTEIN FINANCIAL GROUP

DATA: BUSINESS WEEK

Can a car be two things at once?

Chrysler LHS

Can it be one thing one moment

nd something totally different the next?

t possible?

Nothing is impossible

k a Chrysler engineer

the question:

it a luxury car

sports sedan?

ey will answer.

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Compaq and IBM haven't decided whether to put valu

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Microsoft Windows 95
intel inside
pentium processor

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Cover Story

THE SHREDDER

Did CEO Dunlap save Scott Paper–or just pretty it up

Albert J. Dunlap had just completed the biggest deal of his life. On Dec. 12, Scott Paper Co. shareholders approved his $9.4 billion merger with Kimberly-Clark Corp. amid cheers at Florida's luxurious Boca Raton Resort & Club. "It was almost like a rock concert," says "Chainsaw Al," as he is known to detractors and friends alike. Rather than pop the cork on a bottle of champagne, however, Dunlap went home to his wife, Judy, for what he describes as a "quiet and pensive" evening. "It was a bit of an empty feeling for me," he says. "There was this hollowness there. It was like part of me was gone."

Investors and Wall Street analysts did plenty of celebrating, though. The deal created a $12 billion global consumer-products company. And it represented a professional triumph for Scott Chairman and CEO Dunlap, who has won widespread plaudits for transforming Scott from a stodgy, tired underperformer into a profit powerhouse. Under his leadership, Scott's stock rose 225%, adding $6.3 billion in value to the company. The latest numbers for the world's largest maker of tissue products left nearly everyone dazzled: Thanks to hefty price hikes and deep cost-cutting, third-quarter earnings more than doubled, to a record $155.4 million, surpassing even the rosy expectations of Wall Street.

"WAKE-UP CALL." Dunlap is hardly demure about what he has wrought. "The Scott story will go down in the annals of American business history as one of the most successful, quickest turnarounds ever," he says. "It makes other turnarounds pale by comparison." In the process, Dunlap transformed himself into a high-profile business leader and outspoken champion of the shareholder. "He has been a wake-up call to a lot of CEOs, and he has been good for American business," says Wayne R. Sanders, chairman of Kimberly-Clark.

Little known before his arrival at Scott in April, 1994, the 58-year-old Dunlap has garnered widespread attention and acclaim in the media. He now speaks before MBA students at Wharton and Harvard business schools, and a ghostwriter is hard at work on his autobiography. Headhunters canvas t boards of other sleepy companies that need to be, as Dun so willingly puts it, "Dunlapped."

Much as his brief tenure at Scott did for Dunlap's repu tion, it did more for his personal worth. After less than t years' work, Dunlap walked away with nearly $100 million salary, bonus, stock gains, and other perks. Kimberly-Cl had agreed to pay Dunlap and a corps of his loyal li tenants an extraordinary $41 million in the most lucrat noncompete agreement ever crafted in American busine Dunlap alone got $20 million in exchange for his agreem not to work for a rival for five years, while five senior ex utives pocketed $4.2 million eac

> "Chainsaw Al" brags that other turnarounds pale by comparison. Critics charge that he slashed plenty of muscle along with the fat

But critics inside and outs Scott say Dunlap is leaving the co pany in a much less healthy po tion than he claims. While it is porting record profits and wh investors have reaped big gai Scott is losing U.S. market sh in its three major product fields: per towels, bathroom tissue, and cial tissue (table, page 58). Dun maintains the numbers are "disto ed" because he weeded out num ous unprofitable products. Yet sa numbers in the U.S., according an independent research firm, down in such key brands as C tonelle bath tissue, Scotties facial tissue, and the renam Scott Clean paper towels. In Britain, an important overs market, Scott's share in toilet paper has fallen from 31.5% 26.4% in the past two years, according to A.C. Nielsen Co

Former execs say that's partly because Dunlap cut plenty muscle along with the fat—pumping up short-term resu at the expense of long-term health. More than 11,000 people 71% of headquarters staff, 50% of the managers, and 20% hourly workers—saw their jobs eliminated under Dunlap. the same time, he slashed spending on research and devel ment and staff training. These former executives believe

FETCH: *Dunlap bought a house in Boca Raton, Fla., and moved Scott headquarters there from near Philadelphia*

deep cuts in both workforce and long-term investment will make it hard for Kimberly to achieve the full $600 million in "synergies and cost reductions" that Wall Street is expecting from the combined companies.

What galls many former executives, employees, and union leaders is their belief that Dunlap and his team took credit for improvements that had been in the works for months, if not years. Scott's board of directors began to consider the $1.6 billion sale of publishing paper-maker S. D. Warren Co.—which Dunlap himself calls "the linchpin of my strategy"—in the spring of 1993, a full year before Dunlap arrived. A modern tissue mill in Owensboro, Ky., that Dunlap opened with great fanfare last May had been under way since 1990, when managers selected the site. Several of the new products that Dunlap's team claims responsibility for are the result of years of effort by ousted staffers. Even many of the employee layoffs had already been approved by Scott before Dunlap came on board. Counters Dunlap: "It's one thing to make an announcement. It's another to actually do it."

BROKEN PLEDGE. Then there are the human and social costs of Dunlap's tenure. Besides the thousands of employees laid off, many more were cut loose after Scott sold various pieces of itself. Several communities have lost a generous corporate citizen—especially in the Philadelphia area, where the company was headquartered from its founding in 1879 until last year. Before moving the world headquarters to Boca Raton, Fla.—just after he bought a $1.8 million house there—Dunlap also eliminated all corporate gifts to charities, even reneging on the final $50,000 payment of a $250,000 pledge to the Philadelphia Museum of Art.

The debate over what a company owes its shareholders and what it owes its stakeholders—the people who work for it and the communities in which it operates—is a long-running one, of course. But rarely have the issues been placed in such stark relief as at Scott. Because Dunlap openly revels in his "Chainsaw" sobriquet and loudly trumpets his slashing tactics, he is helping change the norms of acceptable corporate behavior, argues Pe D. Cappelli, chairm of the managem departme at Whart "He is p suading c ers that sha holder value is be-all and end-all," s Cappelli. "But Dur didn't create value. redistributed income from employees and the com nity to the shareholders."

There's no question t before Dunlap's arrival Apr. 19, 1994, Scott Paper a prime example of a morib bureaucracy. Founded by br ers Irvin and Clarence Scot was the first to market roll tissue for use as toilet pa Over the years, Scott bec the world's largest supp of toilet tissue, paper n kins, and paper towels: S grew to $5.4 billion in som countries by 1990. But to competition from rivals suc Procter & Gamble Co. be to erode profit margins as ly as the 1960s. And like m old-line American compan Scott was slow to react.

Enter Dunlap. A W Point graduate and for paratrooper, he has ma career out of being agg sive and decisive. By count, Dunlap has tur around eight ailing compa In the early 1980s, he wo his magic on a badly trou Lily-Tulip Inc. by firing ha headquarters staff and 26 salaried employees. Ther helped Sir James Goldsmith turn around his U.S. operat Dunlap got the nickname "Chainsaw" from a Goldsmith fr who admired Dunlap's ability to cut fat from bloated compa

When Scott's board of directors was looking for a repl ment for Chairman and CEO Philip E. Lippincott, Dul was in retirement. He had quit a job in Australia after years as managing director of Consolidated Press Hold Ltd., the TV and magazine empire owned by billionaire

Two Views of a Turnaround

Scott Paper Chairman Al Dunlap says he has been responsible for "one of the most successful, quickest turnarounds ever." Many former Scott executives and other observers take a different view.

WHAT DUNLAP SAYS

- A key part of his strategy was to invest in Scott for the future
- He went to Scott to run it for the long term—not just to pretty it up for a quick sale to the highest bidder
- Scott launched 107 new products while under Dunlap's tenure
- The "linchpin" of his strategy was to sell printing unit S.D. Warren
- His team claims credit for an innovative product that combines baking soda with bath tissue
- He claims credit for signing joint-production pacts in China, India, and Indonesia to expand the global reach of the company

WHAT OTHERS SAY

- He pumped up short-term results, slashing R&D by 50%
- Dunlap arrived in April, 1994; Salomon was retained later that same year to shop the company
- Many of the "new products" can be accounted for by changes in packaging
- Scott's board had given the O.K. a year earlier to pursue the sale of Warren
- Marketing staffers say they began work on this successful product, a version of Cottonelle, as early as 1991
- The groundwork for the Chinese deal had begun as early as 1988, and the deal might not have been otherwise possible

LOSING GROUND WITH AMERICAN SHOP

SALES IN U.S. FOOD, DRUG, AND MASS MERCHANDISE OUTLETS IN THE 52 WEEKS ENDED OCT. 29

PAPER TOW

TOTAL MARKET	$2 Billion
SCOTT PAPER SALES	$306.6 Million
SCOTT MARKET SHARE	15.3%

Packer. The board's decision to hire Dunlap, Scott's first tside CEO, was made with the expectation of quick action. The board got more than it bargained for. Dunlap brought everaged-buyout mind-set to Scott: slashing expenses, ditch- assets, and paring debt. He showed his impatience with l-fashioned notions of corporate behavior. Touring a Scott ant, Dunlap asked an employee how long he had worked ere. The worker, recalls a colleague, proudly replied that he s a 30-year veteran. "Why would you stay with a company 30 years?" asked Dunlap incredulously.

EACHED WHALE." Within two months of his arrival, he rote a brutal prescription for Scott. There would be ajor changes in management, a restructuring that would minate 35% of the employees, outright sales of units related to Scott's core tissue business, and a new ategy for the future. "Scott was a beached whale," he ys, noting that it had lost market share for four ars in a row, lost $277 million the year before he ar- ed, and had seen its credit standing deteriorate. "Peo- e have to understand that I didn't create the problem."

While Dunlap's cuts went far and ep, he told employees that his goal s to reinvest in the business and shion a clear vision for the future. t many survivors say it soon be- me clear he was interested in sell- out. "At the employee meetings, spoke about building the compa- ," recalls a former marketing ex- utive. "But by the end of 1994, it st became a volume-driven plan to etty up the place for sale."

Dunlap bristles at the charge. hat's pure bullshit," he says, ticking a list of achievements during his ne at Scott: It introduced 107 new oducts last year, signed its first nt ventures in China, India, and donesia, and redesigned its pack- ng worldwide. "It has nothing to with the short term," he says. 'hat I've turned over to Kimberly-Clark is a corporation :h a laid-out strategy, new products, and new facilities." nberly-Clark's Sanders has no doubts about the deal. A okesperson says the merger gives Kimberly far greater ch around the world in a broader range of products. "Now have a stable of some of the best-known brands in the rld," says Tina S. Barry, a Kimberly-Clark vice-president. But of those 107 new products Dunlap points to, nearly half accounted for by changes in packaging of a single product l the upgrading of another. Marketing chief Richard R. olosi concedes that Scott counts as 22 "new products" repackaging of Scott Clean paper towels in 22 countries. other 22 come from upgrading its basic Baby Fresh wet es to a thicker, quilted product in those same 22 countries.

> "Dunlap didn't create value. He redistributed income from the employees and the community to the shareholders"
>
> **PETER D. CAPPELLI**
> *Management Department Chairman, Wharton School*

rnings hit record levels, thanks to sharp cost-cutting, o's Scott has yet to halt a slide in market share

OILET PAPER		FACIAL TISSUE	
4 Billion	up 7.7%	$11.7 Billion	up 5%
Million	up 2%	$77.3 Million	down 2.5%
%	down 1.2 points	6.6%	down 0.5 points

DATA: INFORMATION RESOURCES INC.

Dunlap's boasts about signing joint-production agreements in China, India, and Indonesia also rankle the former executives who laid the groundwork for those initiatives years earlier. The foundation for the joint agreement to produce tissue paper with Shanghai Paper Co. in China, for example, was laid in 1988, when Scott bought a small outfit in Hong Kong, according to a former executive.

Even Dunlap's rhetoric about layoffs doesn't quite match reality. Many of the employee cuts had been approved by Scott's board under Lippincott. "The cutbacks on the hourly side had been agreed to before Dunlap ever came into the picture," says Donald L. Langham, international vice-president for the United Paperworkers Union. "He just rushed up the process."

It's also clear that Dunlap and his top aides began exploring the possibility of selling Scott within months of their arrival. Merger documents filed with the Securities & Exchange Commission show that Salomon Brothers Inc. had been retained in "late 1994" to begin shopping the company. By December and January, Salomon had already identified two dozen potential acquisitors, including Kimberly-Clark.

Beginning in late 1994, former managers say, Dunlap's team began making moves that suggested their time horizons weren't very long. Scott's R&D budget was slashed in half, to about $35 million, and 60% of the staffers in R&D were eliminated. At Nicolosi's behest, the marketing department began weekly volume forecasts, up from monthly reports. "We're talking about a whole new definition of short term," says a former Scott marketer.

The cost-cutters didn't go after just R&D. They also forbade managers from being involved in community activities because that would take away from their business duties. They banned memberships in industry organizations that allowed managers to network with competitors. They also scrapped a yearly event at which Scott met with its leading suppliers to improve relationships and get better prices for goods. Dunlap saw the meeting as a waste. "This was nonsense," he says.

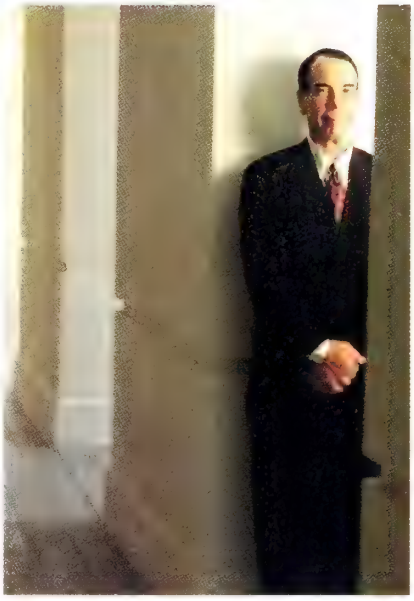
HOGGING THE CREDIT. Former company officials, on the other hand, say Dunlap's take on purchasing was nonsense. The meeting was part of a major reengineering of this function begun in late 1991. Scott winnowed some 20,000 suppliers to about 1,000, knocked off more than $100 million in annual purchasing costs, and wrote up plans for a 75% reduction in the 200-employee department—all before Dunlap arrived. "The numbers were showing up just as Dunlap was coming through the door," says Theodore R. Ramstad, former director of worldwide procurement.

There were still other occasions when the Dunlap forces claimed credit for initiatives begun by their predecessors. One of the most innovative of Scott's new products is a baking-soda-laced toilet tissue, Cottonelle. "It was one of the initiatives that we created and put into the marketplace," boasts Nicolosi, a former P&G executive Dunlap had met on the clay tennis courts of the Boca Raton Hotel and recruited as marketing chieftain. But former marketing staffers say they had been working on this product since 1991. "That did not happen in two months," notes a former executive.

Another claim that doesn't stand up to scrutiny: Dunlap

The Winners

▲ **BASIL ANDERSON** *The chief financial officer walks away with $14.9 million*



▶ **RICHARD NICOLOSI** *A haul of $17.2 million for the marketing chief*

says he was at Scott only one week when he took his ax to the lethargic 11-person executive committee. "I got rid of 9 of the 11, and the other two I gave more responsibility," he says. How did he know so fast whom to fire? "I've done enough of these before," he says. "Each time you do one, you get a little smarter. And after a while, it's almost predictable."

In fact, Dunlap didn't fire any of the 11 in the first week. Three had already announced plans to retire before he arrived. Another three were simply taken off the committee but remained employed by Scott. Four others—including two senior vice-presidents, the general counsel, and the vice-president for human resources—were axed on May 26—five weeks after Dunlap came aboard. Another was let go a month later. "It's a fish story that gets better with each telling," laughs one former member of the committee. Retorts Dunlap: "It was pretty quick."

In their place, Dunlap installed a six-person operating committee. It included three executives he recruited: Russell A. Kersh, who had worked with him for nearly a decade at both Lily-Tulip and under Goldsmith; John P. Murtagh, a lawyer he had also met at Lily and had retained for the Goldsmith group; and Nicolosi, the marketing honcho.

Scarcely a year after they came on board, Dunlap sent senior vice-presidents Kersh and Murtagh to begin merger negotiations with Kimberly-Clark. On June 16, the pair—along with Salomon Managing Director Mark C. Davis, who also worked with Dunlap previously and whose firm gains $28 million on the deal—worked out juicy details of the severance and noncompete payments for Dunlap and five other top members of his team. Kersh, who arrived at Scott in June, 1994, is walking away with $16.4 million. Murtagh, who joined Scott on June 9, 1994, is leaving with $15.9 million. Nicolosi, who came aboard the Dunlap express that August, is getting $17.2 million for 16 months of work. Basil L. Anderson, chief financial officer, leaves with $14.9 million.

BEARING THE BRUNT. All this is salt in the wound to those who have lost their jobs. Jerry Michael Chambless, 49, also worked in Scott's paper plant in Mobile, Ala., for 29 years before being axed as a $60,000-a-year supervisor in the big bloodletting of August, 1994. He has been unable to find another job, is under increasing financial pressure, and a stroke has put him in a wheelchair. "He will never be able to do anything again," says his wife, Marty. The Chamblesses

The Losers

◀ **MICHAEL COLE:** *After 37 years, he was summarily let go—at a much reduced pension*

▼ **MIKE CHAMBLESS** *Axed from his job, he has not found other work and a stroke has left him in a wheelchair*

Cover Story

THE MAKING OF A CORPORATE TOUGH GUY

During Albert J. Dunlap's days at West Point, his boxing coach scored cadets on how much leather they threw and how much blood they lost. Dunlap punched up a storm and rarely bled. "He was aggressive and tough to hit," recalls Philip A. Tripician, who roomed with Dunlap. "He fought out of a crouch. And when he hit you, he stung you."

From the boxing ring to the executive suite, Al Dunlap, 58, has followed a remarkably similar strategy. He moves into troubled companies with an in-your-face attitude rare among executives: He attacks and challenges nearly every premise and person in sight. Those who get in his way feel stung by the experience.

His tough, tell-it-like-it-is persona stems from humble beginnings. He was born in Hoboken, N.J., the son of a shipyard worker. As a boy, he delivered papers and hauled crates of soda off trucks. "My parents couldn't afford to send me to college," he says, "so either I got a scholarship or I wouldn't get an education."

"HOTSHOT." After graduating from high school in 1956, he won a spot at West Point. Of the more than 1,000 cadets who reported to the academy that July, Dunlap was among the 608 who made it through through plebe year and "beast barracks," the first eight weeks of verbal hazing. "I didn't like it," says Dunlap. "You had to be a total masochist to like it, but I knew I had to survive."

Although hardly a stellar student, Dunlap got by on toughness and humor. "He kept things light," says Ken Sindora, a fellow cadet. "He had a hotshot attitude, but he kept us laughing." More important, says Dunlap, "West Point made me tenacious and very organized. It gave a poor little nothing kid a chance to get a very good education, and it opened up worlds I didn't even know existed."

He left the Army in 1963 after a mandatory three-year stint: There was no action available, no war to fight. He joined Kimberly-Clark Corp. as a $7,800-a-year trainee. He learned the paper industry's basics at Kimberly and Sterling Pulp & Paper Co. before becoming an itinerant troubleshooter at Manville, American Can, and Lily-Tulip. In 1986, he emerged as an aide-de-camp to British billionaire Sir James Goldsmith.

POINT MAN: *The academy made Dunlap "tenacious"*

Sometime during his five-year stint with Goldsmith, Dunlap reinvented himself as a champion of the shareholder. He helped lead the attack on Goodyear Tire & Rubber Co. management when Goldsmith made his unsuccessful hostile takeover bid. Dunlap charged that the company wasn't doing enough to maximize shareholder wealth—a situation he also found and has corrected during his 20-month tenure as chairman of Scott Paper Co.

Dunlap bristles at the notion that a business should be run for such stakeholders as employees and communities. "Stakeholders are total rubbish," he says. "It's the shareholders who own the company. Not enough American executives care about the shareholders."

The former cadet hopes to put his philosophy to the test at another company soon. Friends say Dunlap has turned down a few job offers, but they expect him back in the ring shortly.

By John A. Byrne in New York

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ir two children, 7 and 10, are living on Social Security pay-
nts of $12,000 a year and may have to sell their house.
Another Mobile employee, Emory Michael Cole, 58, had fol-
ed his dad's footsteps, joining Scott's labor pool at $1.72 an
r on Nov. 17, 1958. Four of the seven boys in the Cole
ily had worked for the company at one time or another.
er 37 years, Cole worked himself up to a supervisory job
a $72,000-a-year salary. On Aug. 16, 1994, he was called in
n vacation and fired. "I wanted to work four or five more
rs to get my full retirement, nearly $4,000 a month," he
s. Instead, he'll get a monthly pension of $2,670.

LLOW CORE." Dunlap says he is not insensitive to the pain measures have inflicted. "People say I've made a lot of ney off the backs of people by cutting all these jobs," he s, "I find that personally offensive. I come from a working-s family, a father who was a union steward at the ship-ls and a mother who worked in the five-and-dime. If I e to get rid of 35% of the people to save 65%, that's t I am going to do. It was me or Dr. Kevorkian."

roblem is, the 65% who survived don't feel much as if were saved. The day after the merger's completion, Kim-y-Clark said it would cut 8,000 of the combined companies' 00 workforce by 1997. Among other things, Kimberly said it would shutter Scott's headquarters in Boca Raton—an announcement it made the same day that local officials received Dunlap's request for a $156,000 incentive grant for job creation.

His supporters insist that what ultimately counts is the $6.3 billion in value that Dunlap created. Some of the stock's rise, however, can be attributed to Wall Street speculation that the company would be sold. The day Dunlap's appointment was announced, a highly respected Brown Brothers Harriman & Co. analyst, Kathryn F. McAuley, ran a check on his previous experience. Recalls McAuley: "I said to myself: 'Well, the board sold the company.' When you looked at his background, you realized that what he had done best was sell companies."

In any case, Dunlap's "empty" feelings on his day of celebration are probably shared by thousands of other Scott employees. "His sentence should be to run the company as it is for five years," says a former high-level Scott executive. "He would never be able to do it. Scott is just a hollow core." Kimberly-Clark Chairman Sanders may have been right when he said Dunlap had been a wake-up call to a lot of CEOs. But the lesson to be drawn from his tenure at Scott may not be quite the one Sanders had in mind.

By John A. Byrne in New York, with Joseph Weber in Philadelphia

IN THE AGE OF THE VIRTUAL OFFICE

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STRATEGIES

THE PRESS OF NEW BUSINESS

Printer Donnelley thrives by seizing electronic tools

As he walks around a splendid Gothic-style library at the Chicago headquarters of R. R. Donnelley & Sons Co., John R. Walter proudly points to museum-quality material—everything from Ming Dynasty currency to leaves from *The Canterbury Tales*. The 48-year-old chairman pulls out an inaugural issue of *Life* magazine dated Nov. 23, 1936. But as he turns the aging pages, he says, with a trace of irony: "This isn't relevant anymore."

In recent years, Walter and his top managers have wondered whether Donnelley, the world's largest commercial printing company, was still relevant itself. In a world that's becoming increasingly dominated by software, electronic publishing, and the Internet, they worried that traditional ink-on-paper printing might be facing a gradual but inevitable obsolescence.

Now, those worries appear to have been premature. The company is thriving, thanks to Walter's two-pronged strategy: Donnelley is taking advantage of high-tech and electronic publishing tools to increase its share of the mature U.S. market while bolstering its position in the still-lucrative traditional print business in developing countries. Early this year, the company will begin a series of big new contracts, ranging from the printing of phone books in China to a huge 10-year pact to print 15 million copies a month of *Reader's Digest* in the U.S. Indeed, growth in its magazine unit—which prints *Time*, *Newsweek*, and BUSINESS WEEK—and growth in catalogs and phone books helped boost Donnelley's 1995 sales an estimated 31%, to $6.4 billion, and earnings 12%, to $301 million, figures James D. Dougherty of Dean Witter Reynolds Inc. He expects sales to jump a further 18% this year, to $7.6 billion, and income to rise 17%, to $353 million.

EXACT AIM. Yet Donnelley's future does indeed lie in the digital era. Walter talks of transforming the old-line printer from a manufacturer to a marketing-and-services company able to provide customers with editorial products in whatever format they want—from magazines to software disks and online material. "We will take any kind of content to the end-user," says Walter.

In fact, technology that once seemed so threatening is now strengthening Donnelley's ties to customers. A longtime printer of Microsoft Corp. software manuals, Donnelley is now one of the top duplicators and wholesale distributors of software disks for Windows 95. And insiders at *Reader's Digest* say Donnelley won the contract to print the American edition from Quebecor Inc., a Montreal rival, after agreeing to invest in new computerized sorting equipment at its Lancaster (Pa.) plant. The gear allows the publisher to aim promotional inserts or ads at specific groups or neighborhoods. While Walter figures that the rise of software and other market trends could make 25% of Donnelley's business obsolete, "the opportunities created by technology far outweigh the risks," he says.

Mixed media: Donnelley is a leading duplicator of software—and is also bolstering its position in lucrative magazine printing

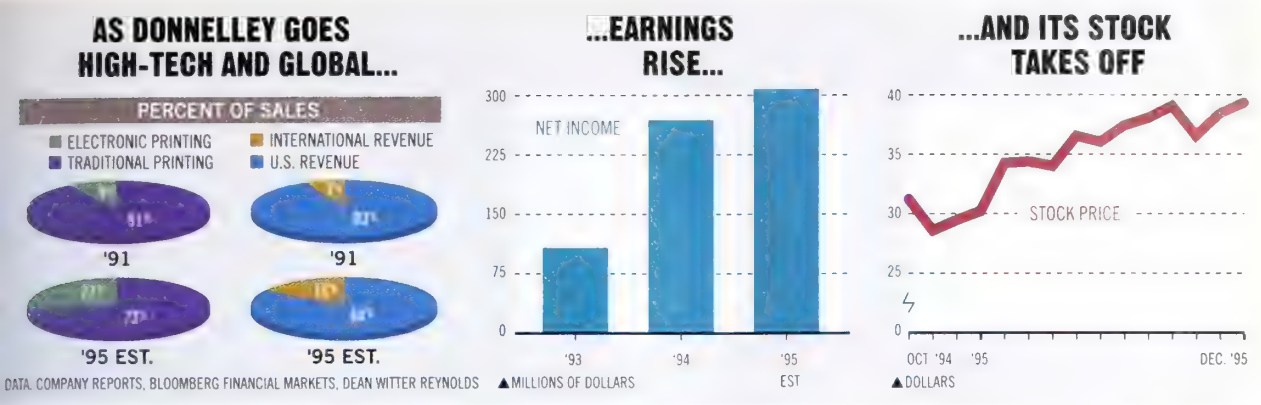
WALTER: "WE WILL TAKE ANY KIND OF CONTENT TO THE END-USER"

But that means heavy spending: Over the past two years, Walter has invested roughly $225 million annually on new technology. In mid-1995, Donnelley acquired Corporate Software Inc., then merged it with its own Global Software Services. Now renamed Stream International, the $1.5 billion software producer, distributor, and consultant represents 23% of sales, up from an 8% sliver five years ago. Stream is growing at 25% annually and this year is poised to ove take catalogs as Donnelley's largest di sion. Its traditional business is getting high-tech gloss, too: Donnelley opened digital printing plant in Memphis th allows it to download information rectly from customers and print targ ed catalogs and promotional materi the same day.

THREAT OVERSEAS. To be sure, Donn ley isn't the only old-line printer goi electronic. Rivals such as Quebecor, Ba ta, and Quad Graphics are also maki the shift. But the sheer scale and ran of Donnelley's services—funded by nual cash flow of roughly $700 millior are winning kudos from customers. " of the printers have access to the sa technology, but Donnelley understar the full implications of how we mig market our products," says Steve Joss, vice-president for marketing

Capital Cities/ABC Inc.'s Agricultu Group. Joss now has 19 magazines der contract with Donnelley. Donne turns out thousands of variations some of the titles, tied to data such the size of subscribers' farms.

Investors have certainly cheered he shift. The company's return on equ had averaged nearly 17% in the mi 1980s—but early in the 1990s it fell to 13.5%. The stock mostly moved sideways, trading around 30 until late 19 "Operating results never quite matched the rhetoric," says Dean Witt



ugherty. Now, analysts expect ROE return to nearly 17% by 1997, up m around 14.9% in 1995. Over the st year, Donnelley's shares have mped 33%, to 39%. Says E. Wayne rdberg, an equity partner at Lord, bett & Co., a Donnelley shareholder: hey have become much more masters of their own destiny."

Overseas, too, Donnelley is becoming

e of a eat. Over past two rs, Walter poured an mated $300 million into four ven- s abroad. He has steered clear of well-established heavyweights in de- ped markets. Instead, he's aiming ap developing countries that have literacy rates and a growing middle , where conventional printing is still owth business. Donnelley has ac- ed a 51% stake in Chile's Editorial l Cochrane and a 25% stake in In- Tata Press Ltd. It converted a military-jet hangar in Krakow, Poland, into a 350,000-square-foot printing plant and built a new facility in Shenzhen, China. Baltimore's Waverly Inc., a $140 million medical-book publisher, is eyeing Donnelley's Chinese and Polish plants as a springboard for its own expansion.

Such moves have pushed estimated international sales to 16% of the total, up from 7% five years ago. While Europe is crowded with printers, Hans Preising, an official at the print and publishing arm of Bertelsmann AG, says the German giant is taking "special note" of Donnelley. "It is making its way onto the marketplace with power and force," he says.

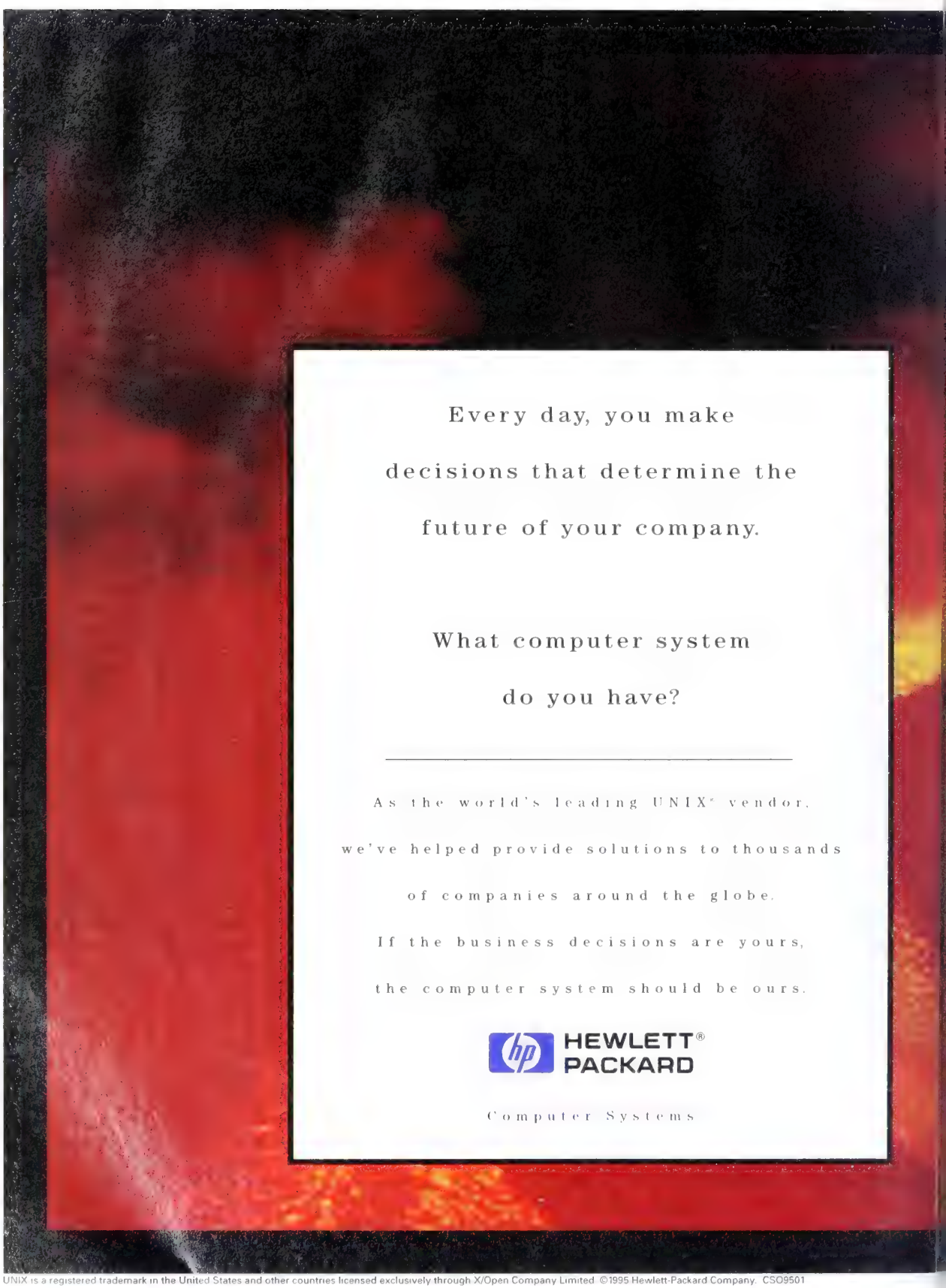
Much of the credit for the remake goes to Walter. Intense, hypercompetitive, and self-confident, Walter rose to the presidency at 39 in 1987 after stints in sales and manufacturing. He recalls asking one former chairman "to promote me until I fail. I don't want to be held back because of my age." When Walter became chairman and CEO two years later, he took over a company that insiders have described as bureaucratic, slow-moving, and beset by regional rivalries.

NIMBLER. Walter quickly set a new tone. He pushed contract negotiations and pricing decisions away from headquarters and into the hands of business-unit managers, and he urged them to spend more time with customers and employees. "This used to be a militaristic, autocratic operation where much of the management team and hourly workforce were administrators," says Jonathan P. Ward, head of the commercial printing unit. "Now, we're expected to make decisions."

Still, it's hard to make a company of Donnelley's size very nimble. Although Lee E. Krubner, vice-president for operations at a Waverly unit, generally lauds Donnelley, he also says the company's marketing thunder sometimes exceeds its ability to deliver. "They move into markets with the brute force of a [$6 billion] company," says Krubner. "They can tell the right story, but getting all the pieces to work together takes time." Warns Harry V. Quadracci, CEO of $1 billion privately held Quad Graphics Inc.: "Donnelley's challenge will be dealing with size. They'll see smaller companies that are more flexible and guerrilla-like in their sales." Quadracci says he has picked up contracts from publishers that became wary of a growing Donnelley dominating the market.

It's a dilemma that Walter insists he's well aware of. "Size can be our greatest asset," he says, "but it can also be a big problem if we are not nimble and fast." If he can continue to bring about change at the company, he's certain to ensure Donnelley's future, even if its printing presses one day end up in a museum.

By Richard A. Melcher in Chicago



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CONGRESS

DISCOVERED ALIVE: GOP MODERATES

In fact, they've actually managed to rein in the Newtoids

Last August, House Speaker Newt Gingrich (R-Ga.) faced an insurrection. A cadre of Republican moderates, led by Representative Sherwood L. Boehlert of New York, was threatening to block GOP plans to slash spending for Labor Dept. job training and to kill heating-bill subsidies for the poor. "I know you are unhappy," Gingrich told the rebels in a private meeting, recalls Boehlert. Then, Gingrich conceded that passage of the appropriations measure didn't have a chance without their backing. Gingrich hinted he would push for more funding. With that, the moderates fell back in line. Now, the final bill seems likely to preserve heating aid and some job training for at least another year.

While a noisy group of far-right freshmen has been getting all the attention, a quiet but persistent bloc of about 30 centrist Republicans has been surprisingly successful at actually getting things accomplished. Although they remain a minority within the strongly conservative House GOP caucus, the moderates have emerged as a critical swing bloc. The key to their leverage: threatening to team up with the 197 Democratic members to rein in the Republican revolutionaries.

The bloc's proudest achievement is a series of environmental victories in 1995 that thwarted GOP hard-liner attempts to junk clean-water laws and curb Environmental Protection Agency enforcement powers. "The moderates have really been sticking their necks out," says Paul Brotherton, research director of the League of Conservation Voters. "They've helped tremendously in stemming huge [environmental] losses."

The triumphs don't end there. The moderate bloc is also credited with forcing Gingrich & Co. to target cuts to middle-income parents, sav the Corporation for Public Broadc ing, and scuttling a business-backed to repeal the Davis-Bacon Act, wh requires federal contractors to workers at prevailing union rates.

Emboldened by its influence, the trist group is now gearing up for a rescue mission. Among their objecti salvaging Amtrak subsidies, aid to arts, and family-planning funding. we stick together, we can be a for says Representative Marge Rouke (R-N.J.). "We shouldn't be balanc the budget on the backs of the sick, elderly, children, and the disabled."

Sounds almost liberal. But the publican rebels have succeeded wh Democratic dissidents failed beca they are unquestionably loyal to party and its top priority: a balan budget in seven years. Although s House leaders de these career b benchers as be "squishy" becaus their eagerness compromise, t work smoothly v the Speaker. "(grich has discove that we are g team players," s Boehlert, a lead centrist who readily admits he'll t controlling the House over mino status any day. The hitch? "I am vinced that we will be in the majo for the next generation if we so some of our hard edges and don't t our back on the environment."

TRUMP CARD By threatening to undo the slim GOP majority, Boehlert and his bloc exert leverage beyond their numbers

GRIM DAYS. Success for Boehlert ha been easy. In early 1995, the New Y er mustered only one other GOP against the Contract With Ameri sweeping deregulation plan. "Am I last moderate Republican?" he lamen at the time. Since then, the gro ranks have swelled along with polls show most voters consider the Ging agenda too extreme. Nowadays, the plots strategy at a weekly Tues Lunch Bunch headed by Represe tives Frederick S. Upton of Michi and Steve Gunderson of Wisconsin.

Some GOP colleagues bristle at moderates' clout. To counteract t gains, hard-liners have organized a member Conservative Action T (CAT). "They're off-base on a numbe issues," scoffs Representative Dan I ton (R-Ind.), one of CAT's top dogs. the centrists' influence is no joking m ter to Burton. "The moderate-to-lib members of the party were startin

WHERE REPUBLICAN REBELS WIELDED CLOUT

ENVIRONMENTAL ISSUES Blocked efforts by conservatives to scrap clean-water laws and limit Environmental Protection Agency enforcement.

TAX CUTS Successfully argued that Republicans should target their child tax credit to middle-income families and exclude families earning more than $110,000 a year.

PUBLIC BROADCASTING Scuttled plans to scrap funding for the Corporation for Public Broadcasting, winning modest cuts instead.

FAMILY PLANNING Prevented hard-liners from eliminating federal assistance to groups that provide family-planning advice.

DAVIS-BACON Stopped a plan to repeal the Davis-Bacon Act, which requires federal contractors to pay workers at prevailing union rates.

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ntroller. "There was a time when we
l to do things manually. But today,
can review many aspects of our busi-
s just by pointing and clicking."

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r of Information Services for Purina
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rmation to managers as quickly as
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arch, and as a management support
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me, and comparative analyses
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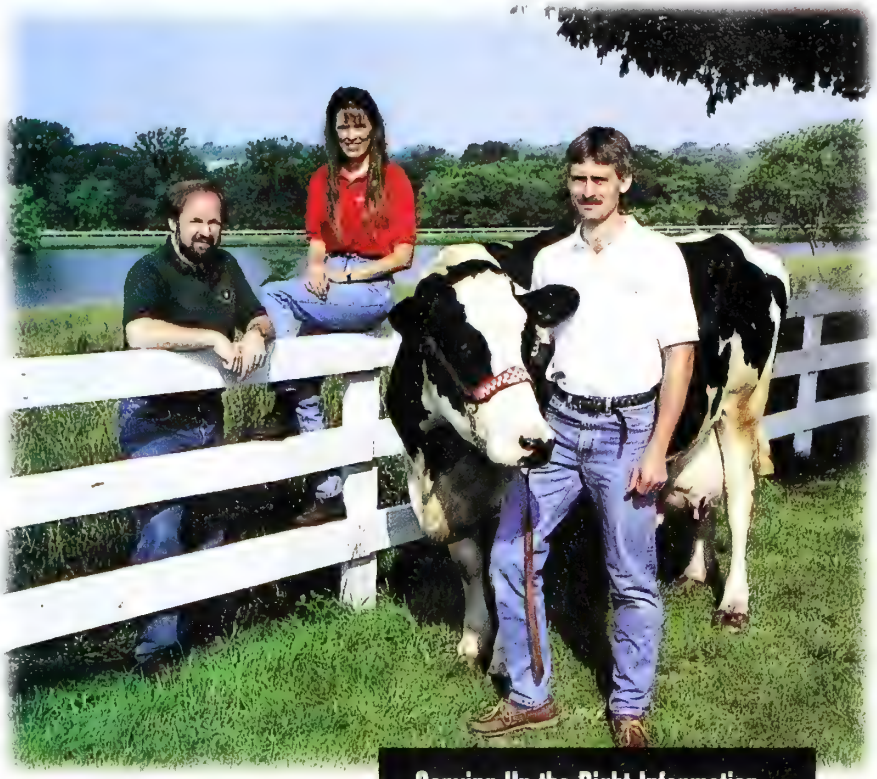

Daignault, Brown, Durbin

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Connie Brown, Purina Mills Information Analyst, says the key business benefits of using the SAS System are "improved productivity by key field management and a consistent thought process in the use of management information. There is no question that field management spends less time gathering numbers and more time using good information to support the decision process. Mapping and graphical presentations are becoming more important in the decision process, and SAS Institute has been very supportive in helping us implement these tools."

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have too big an impact on the leadership," he says. "If the liberals start to push the party in the wrong direction, we think it is incumbent upon us to make sure this doesn't happen."

That's why incensed right-wingers are warning House leaders not to kowtow to the centrists—even if it means the defeat of some GOP initiatives. "They are holding the majority hostage," grouses L. Brent Bozell III, chairman of the Conservative Victory Committee, an activist group. "Conservatives should fight for principles. You might lose a battle, but you'll win the war."

To bridge his party's ideological divide, Gingrich has created a Contentious Issues Group to seek consensus on such flash points as the Endangered Species Act and legal aid for the poor. So far, thanks to the budget impasse, CIG's bridge-building has been put on hold. But the players are hopeful. Explains Burton: "We either start shooting each other or try to hammer it out."

But some battles will be unavoidable, and the centrists show no willingness to buckle. Indeed, many are cool to tax cuts. And Boehlert expects more skirmishes over regulatory reform, environmental enforcement, education, job training, and safety-net programs for the poor and elderly. "We want to demonstrate that government is not all bad," he says. "Most of it works well."

RECRUITING. Such talk drives GOP revolutionaries crazy. But as President Clinton's surging poll numbers show, striking a moderate pose against excesses of the left and the right seems to be a winner with mainstream voters right now. And if the ranks of the Newtoids are thinned come November, the clout of Boehlert's gang could grow in 1997. Already, they are trying to expand their numbers: They boosted the recent special election campaign of moderate Representative Tom Campbell (R-Calif.) by collecting endorsements from environmental groups.

For now, a key part of their plan is to keep hot-button issues like abortion and gun control off the GOP agenda, as they recently did when they helped block a planned vote on lifting the assault rifle ban. The moderates—generally supporters of Presidential hopeful Bob Dole—hope new polls and the voters will "send a message to the leadership that it is suicidal to push some of the more right-wing aspects of the agenda," confides a Boehlert staffer.

Whether the moderates can win this battle for the Republican soul remains to be seen. But they're confident that smoothing the GOP's harsher edges gives their party its best shot at retaining control of Congress for years to come.

By Richard S. Dunham and John Carey in Washington

SO FAR, BORIS SMIRNOFF HAS BESTED HEUBLEIN IN RUSSIAN COURTS

TRADEMARKS

WHO OWNS THE SMIRNOFF NAME?

In the post-Soviet era, an heir contests Heublein's rights

Boris Smirnoff's decaying office, located across the river from the Kremlin in Moscow, is in the same building that housed his great-grandfather's world-famous vodka business more than a century ago. The walls are decorated with black-and-white photos of ancestors, including Pyotr Smirnoff, founder of the Trade House of P. A. Smirnoff, as well as with prerevolutionary advertisements used to promote Czar Alexander III's vodka of choice. And now, almost 80 years after Bolshevik rulers stripped the Smirnoffs and all other Russians of their private property, Boris has launched a series of legal assaults to reclaim the family spirits business. "We have 287 recipes, and we are going to produce them," says the 37-year-old onetime KGB officer.

The problem is that Boris' lineage may not be enough of a claim to let him pick up where his ancestors left off. In the intervening decades, since 1939, Heublein Inc., a subsidiary of London-based International Distillers & Vintners (IDV) and its parent, food giant Grand Metropolitan PLC, became the exclusive distributor of Smirnoff vodka. The company says it paid $14,000 for the rights to the Smirnoff name from an American businessman who acquired them in 1933 from Vladimir Smirnoff, one of Pyotr's three sons. Today, the brand is worth an estimated $1.4 billion.

With registered trademarks in 138 countries, Heublein isn't about to give up the brand that is outsold only by Bacardi rum. "We acquired the rights in good faith and subsequently built the brand through our efforts and investments alone," says Heublein spokesman Jack Shea. "Boris Smirnoff is simply attempting to profit from the enormous investments Heublein has made." Shea estimates that Heublein has spent "hundreds of millions of dollars" over the past 50 years plugging the Smirnoff brand. In 1995 alone, he says, the company poured more than $10 million into advertising just in the U. S.

The contested ownership of the Smirnoff brand is one of a growing number of legal battles in the U. S. and Russia. The cases could signal the way in which post-communist Russia addresses an increasingly familiar problem: Who owns the rights to former Soviet state enter-

prises? "Where is it that you draw the line with respect to restoration of private interests?" asks Jeffrey A. Burt, a Russian-law expert at Arnold & Porter in Washington. "Everything in the entire country was owned by somebody before the revolution."

Other former communist-bloc countries have tried to deal with reclamation issues by passing new intellectual-property laws or by paying nominal amounts to individuals whose property was seized. That hasn't solved every problem. Anheuser-Busch Cos. has been fighting in the Czech Republic for years over the Budweiser beer trademark. But in Russia, virtually all heirs seeking rights to prerevolutionary possessions must resolve their disputes on a case-by-case basis.

FAMILY SPLIT. Consequently, a diverse and growing number of claimants is taking the offensive. World-renowned cellist Mstislav L. Rostropovich, for one, has sued two U.S. companies for selling recordings made in the 1960s before his defection to the U.S. The Anglican Church is trying to regain ownership of a church in Moscow now used by a recording studio. "There's the potential for a huge amount of litigation and mischief," says Michael A. Epstein, an intellectual-property lawyer in New York. "The Communist government appropriated all sorts of inventions and businesses from individuals." Adds Oleg Garsov, director of the Society of Russian Merchants & Industrialists, a group that tries to protect owner interests: "The problem is that there are no laws."

Boris Smirnoff and his American business partners aren't deterred—at home or abroad. On Dec. 8, they sued Heublein for fraud and consumer deception in a Delaware federal court in an effort to invalidate the company's U.S. trademark. The argument: Vladimir had no right to sell the Smirnoff trademarks back in 1933, because he already had sold his stake in the family business to his brother in 1904—for 500,000 rubles. Therefore, they claim, Heublein's use of the brand and its various quality awards, emblems, and medals has been based on a fraudulent transaction. "Heublein has misled generations of Americans into believing that their vodka has something to do with Pyotr Smirnoff," says William N. Walker, president of Russian American Spirits Co., an outfit that hopes to sell Smirnoff vodka in the U.S. and elsewhere.

Walker and Boris Smirnoff are so confident of their position that they have invited the 10 largest international spirits companies to bid by Feb. 16 for the rights to market Smirnoff vodka in Russia. They're charging $50,000 up front just to participate in the auction.

Their optimism has some basis. On Sept. 11, a court in Krymsk, Russia, declared Heublein's use of the Smirnoff trademark to be unlawful and barred the company from making any claims that its products are related to the original Smirnoff vodka, including its treasured distinction as the "Official Purveyor to the Russian Imperial Court." A court in Krasnodar upheld that decision on Dec. 19. In addition, the Russian Patent Office Chamber of Appeals has invalidated Heublein's trademarks.

Heublein and its big-name owners concede nothing, however, and vow to appeal the decisions. That's not surprising given that Smirnoff is the companies' single largest liquor brand, selling some 15 million cases worldwide. Heublein is banking on three key arguments to prove that its ownership is legitimate.

First, Heublein contends that Vladimir had every right to sell the Smirnoff name when he did. After the Bolshevik revolution, the trademark, like many others, was abandoned by the Soviet government. That left Vladimir, who had fled, free to revive the business in Poland. "There was nobody else from whom to acquire the Smirnoff rights," says Heublein's Shea. "The company was dormant after the revolution."

In addition, through the three-year-old Smirnoff Foundation, funded by Heublein and its parent companies with $200,000 annually, numerous family members have been tracked down who oppose Boris' crusade. IDV says that so far, 34 Smirnoffs have signed declarations stating that they back Heublein's claims and object to what they view as Boris' selfish efforts to win exclusive rights to Pyotr Smirnoff's legacy. "Justice will prevail, and the undertaking of Boris will finally collapse," says Kira Vladimirovna Smirnova, a direct descendant of Vladimir who admits to receiving a small salary as an employee of the foundation. An IDV spokesman denies buying the support of Smirnoffs and notes that only half of the signatories have received compensation from the company—most of them earning "less than five-figure sums" annually.

GOLDEN LABEL: *A brand valued at $1.4 billion*

CRUCIAL CONNECTION. Last, Heublein argues that Boris Smirnoff is not entitled to take control of a product that it has largely created through marketing campaigns and other investments. Smirnoff was selling 5,000 cases a year in the U.S. when Heublein first took over the brand. In 1995, the company says it sold more than 5 million cases. "It's a well-established principle that if one claimant lets a [trademark] sit fallow and another puts a lot of energy and investment into it, then that can be the basis for awarding the mark to one claimant over another," says Michael A. Newcity of the Center for Slavic, Eurasian & Eastern European Studies at Duke University.

Heublein had better hope that courts in the U.S. and elsewhere see it that way. Industry experts say the company would have difficulty holding onto market share if it loses its connection to Pyotr Smirnoff. "It's a little bit like finding out that your mom and dad aren't your real mom and dad and that you were adopted," observes Tom Pirko, president of Bevmark PLC. "It's hard to come up with a value for the brand if it can't claim that Russian heritage anymore." That seems to be the one thing on which both sides agree.

By Linda Himelstein in New York, with Peter Galuszka in Moscow and Julia Flynn in London

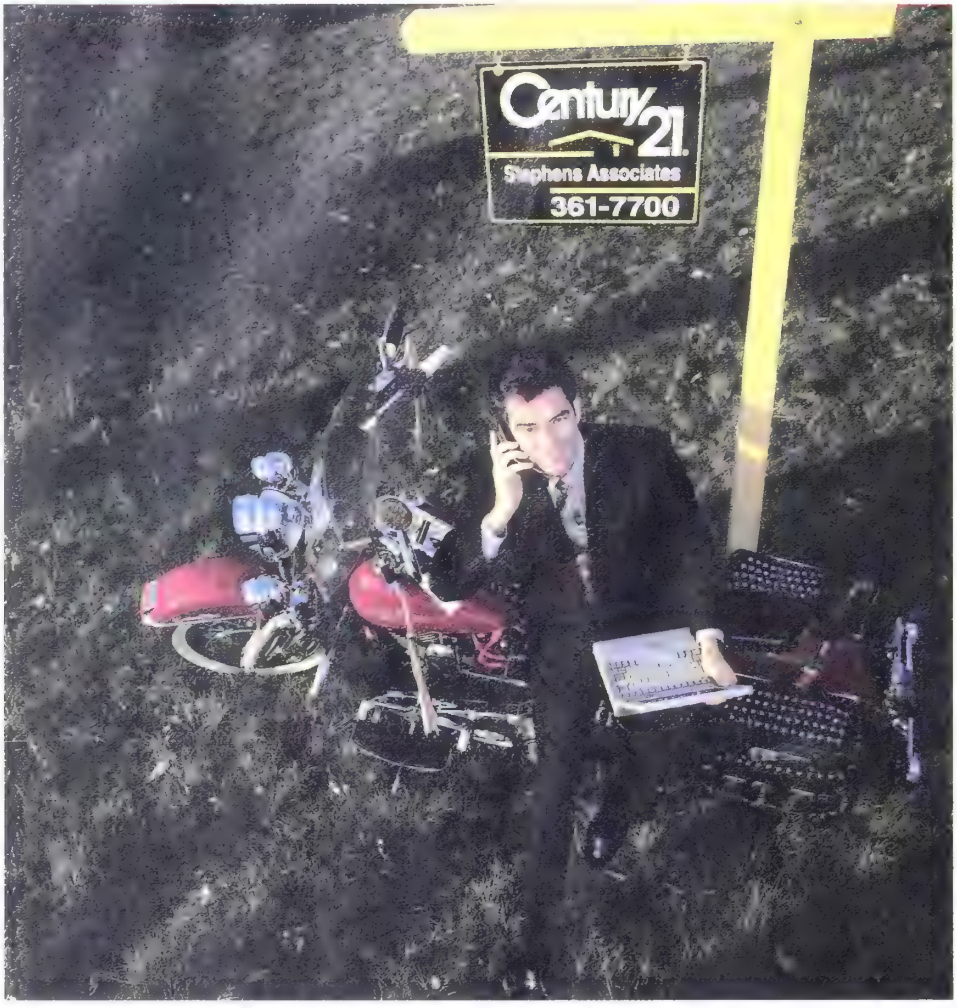
PRIVATE PROPERTY—WHAT'S THAT?

Heublein's trademark dispute raises important legal issues in post-communist Russia:

OWNERSHIP With the collapse of the Soviet state, ownership of some property and former government enterprises is up for grabs. Should they belong to citizens, descendants, émigrés, or deep-pocketed companies?

STATUS OF INTELLECTUAL PROPERTY Under communism, many patents, copyrights, and trademarks remained unused. Are those rights still valid years after foreign interests have assumed control?

CREATING VALUE Prerevolutionary businesses had a certain value. But are would-be inheritors entitled to those businesses after foreign investments in marketing have greatly increased their value?



REAL ESTATE

I WANT MY CENTURY 21!

MTV's former CEO aims to sell you more than just a house

Leave it to Robert W. Pittman to come up with a catchy rallying cry for his sales force. As the new chief executive of Century 21 Real Estate Corp., Pittman—perhaps best known as a founder of MTV Networks and the man who turned around Six Flags Corp.'s theme parks—shares a simple message with the real estate brokers and agents he meets: "You either make dust or you eat dust." It's vintage Pittman. The 42-year-old entertainment-industry hotshot is out to reshape the Century 21 franchise into a marketing powerhouse. Not only will it sell homes, but Pittman envisions a "virtual home store" able to offer and sign up customers for a wide range of discounted home services—all via an agent's laptop computer.

Until last August, Century 21, a franchise operation of more than 6,000 offices in 11 countries, was owned by Metropolitan Life Insurance Co. "The overall philosophy of companies that own residential real estate brokerages has been to try and push their proprietary products through the system," notes Michael G. Mueller, a lodging analyst with Montgomery Securities of San Francisco. By and large, that hasn't been an effective strategy, he says, because brokers are uncomfortable marketing only one company's product. Century 21 did turn a small profit for MetLife, but "there is only so much capital and so much attention to go around, and it was a distraction," says a MetLife spokesperson.

> "Century 21 is the big sleeping giant of this business."
>
> —BOB PITTMAN, Chief Executive

In August, HFS Inc. paid $200 million in cash and stock for the brand. As the world's largest franchise service business, HFS owns brands such as Ramada and Howard Johnson. It sounds ho-hum, but HFS is a fast-growing, entrepreneurial operation (box).

Pittman is taking a fresh approach to the fragmented real estate brokerage industry. The plan: play on the growing importance of brand names and make Century 21 a one-stop shopping center. "Century 21 is the big sleeping giant of this business," says Pittman. His high-tech vision has homeowners sitting down with an agent and ordering up cable service, appliances, a mortgage, insurance, and so on—all at discounts that HFS has negotiated with vendors. "Century 21 is not about buying and selling houses," says Henry R. Silverman, the CEO of HFS. "It's a marketing and distribution opportunity to the 400,000 to 500,000 people buying homes through us."

"CASH-FLOW MACHINE." First and foremost, Century 21 must convince brokers that there is a solid economic benefit to being affiliated with it. Growth in its franchise system was slight under former management. And "we have yet to see how much these preferred vendor arrangements will contribute to the broker's business," notes Mueller. But with an aggressive new management and a market share nearly three times that of the next competitor, and growing,

Pittman has a powerful lure for new franchisees.

When Silverman needed someone to implement his grand plan for Century 21, he turned to Pittman. He had met Pittman in 1990 when the two worked on a joint venture between Pittman's employer, Time Warner Inc., and the Blackstone Group, where Silverman was general partner, to buy Six Flags. He was impressed: "When Pittman started at Six Flags, cash flow was $100 million," he says. "When it was sold 3½ years later, cash flow was $170 million."

The concept at the heart of the plan to reshape Century 21 is the same one that has made HFS what analysts call "a cash-flow machine." The idea: build a network of preferred vendors that gain market share and access to Century 21 customers in return for fees that are split between HFS and franchisees and volume discounts. At the same time, increase brand name awareness and revenues by inking licensing deals for the Century 21 name.

The pieces appear to be falling into place. In October, 1995, the company signed a 20-year licensing deal with a Dallas-based home improvement chain, AMRE Inc. AMRE had been the biggest licensee of Sears, Roebuck & Co., operating as Sears Home Improvement Centers. AMRE will now operate under the name Century 21 Home Improvements and pay Century 21 annual fees of $11 million or 3% of revenues, whichever is greater. Brokers making referrals to AMRE that pan out earn referral fees.

AGGRESSIVE ADS. A steady stream of deals has been announced in recent months. Century 21 franchisees now get a volume discount from AT&T and can offer discounts on cars through an agreement with Potamkin Fleet Sales of New York, a large General Motors Corp. dealer. The brand name will get more exposure through a deal with a book publisher for a series of how-to guides for homeowners, a joint venture to launch a revamped magazine, *Century 21 House & Home*, and a deal with GE Capital Consumer Card Co. to issue co-branded credit cards using the Century 21 and HSF hotel brand names.

Also in the works are deals with mortgage lenders, home-security companies, and online services. Pittman developed technological expertise during his tenure as head of Time Warner Enterprises. He currently serves on the boards of America Online Inc. and 3DO Co., a company focused on interactive multimedia.

Implementing technology across the vast franchise network may prove difficult. "What HFS and Century 21 are trying to do is take existing technology and push it into a business that hasn't been very receptive to it," says Steven M. Friedman, director of the housing segment of E&Y Kenneth Leventhal Real Estate Group. HFS's recent acquisition of Electronic Realty Associates, a pioneer in applying technology to the real estate business, may give Century 21's efforts a jump start.

Pittman's most visible salvo will be an aggressive national ad campaign. At MTV, Pittman had the "I want my MTV" slogan, and at Six Flags, he had "Bigger than Disney and closer to home." Pittman says he will unveil a "high-impact" slogan in the next few months. "The current advertising is too generic," he says. "I want our advertising to be more of a call to action."

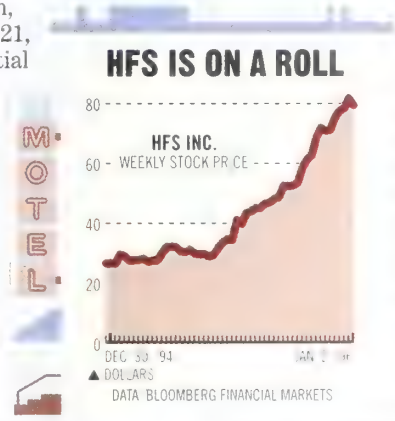
It's too early to tell if Pittman can turn Century 21 into a marketing powerhouse. But Pittman, who flies airplanes and rides Harley-Davidson motorcycles in his spare time, has a way of moving companies into the fast lane.

By Suzanne Woolley in New York

HOTELS CALL THEM FOR ROOM SERVICE

For Henry Silverman, 1995 was a great year. His company, HFS Inc. of Parsippany, N.J., saw its stock price triple. But Silverman, the largest single shareholder of HFS, isn't wasting time patting himself on the back. After becoming a dominant force in the hotel industry, he is setting his sights on the home-sales and -services business.

HFS is the franchisor of lodging chains such as Howard Johnson, Ramada, and Days Inn, as well as Century 21, the leading residential real estate brokerage brand. "We are a service provider... and our commodity is brand marketing and brand assurance," says Silverman. HFS provides franchisees with ad campaigns, reservation systems, training programs, and other support.



But in addition to getting a straight fee from franchisees, HFS negotiates deals with vendors such as AT&T and Pizza Hut that bring in additional revenue to both itself and the franchisee. Morgan Stanley & Co. analyst Neil Barsky, who has a "strong buy" rating on HFS's stock, uses the example of a traveler checking into an HFS hotel and taking advantage of a Pizza Hut coupon in the room. For every pizza ordered, HFS gets 50¢ and the franchisee gets 50¢. The franchisee and HFS get extra income, the traveler gets their pizza, and Pizza Hut presumably gains market share.

Such programs have helped HFS's earnings achieve a 48% compound annual growth rate since going public in 1992. "The truly different thing HFS has done in lodging is to use their buying power to negotiate deals with so-called preferred vendors," says Michael G. Mueller, an analyst for Montgomery Securities. "It generates enormous cash flow and requires no capital spending."

ON THE PROWL. Silverman recently added to his stable of brands by agreeing to buy Electronic Realty Associates and its home-warranty business for $46 million. ERA will be managed as a brand separate from Century 21. But together, the brands have a 15% market share. And Silverman is on the prowl for other residential real estate brokerages.

Silverman's career has not been without controversy. His history of rapid-fire dealmaking includes profiting from buying and selling the Days Inn chain a number of times. The first time was in the mid-1980s, when he was CEO of Reliance Capital Group, a venture-capital subsidiary of Reliance Insurance. In 1990, he became general partner of investment firm Blackstone Group, where he ran an $850 million buyout fund that was the genesis of HFS. In 1992, when part of HFS was sold to the public, Silverman became its chairman and CEO.

Judging from analysts' earnings estimates, HFS has a bright future. The consensus earnings estimate for 1996 is a 44% increase from 1995. For Silverman, 1996 could be another great year.

By Suzanne Woolley in New York

AIRLINES

A PEOPLE EXPRESS FOR THE 1990s?

Bill Hambrecht launches another no-frills, high-risk carrier

Taking fliers on Genentech Inc. and Apple Computer Inc. made William R. Hambrecht a fortune. When it comes to airlines, however, the cofounder and chairman of Hambrecht & Quist Group Inc., the San Francisco investment bankers, hasn't much to brag about. After H&Q underwrote the 1980 initial public offering of People Express Airlines, the stock soared. But the airline folded in 1986, and stockholders lost a bundle. Well, today Hambrecht has returned to the skies—and they are starting to look as cloudy as they were a decade ago.

McADOO: *Charting a course around the major carriers*

Once again, Hambrecht is the underwriter and lead shareholder of an airline—and it's a virtual clone of People Express. It's called Vanguard Airlines Inc., and it's based in Kansas City, Mo., far from People's old Newark (N.J.) hub. But the differences pretty much end there. Like People, Vanguard is a low-cost, no-frills carrier, and it has some of the same executives—such as chief executive officer Robert J. McAdoo, who was chief financial officer of People. Like People, Vanguard has begun to encounter some turbulence—and Wall Street has taken notice. Vanguard's shares have languished in recent weeks (chart).

TOUGH ODDS. Does Vanguard have a better chance of success than its ill-starred predecessor? Hambrecht is hanging in there. "I decided to try it one more time," he says, "to see if it works." Still, the odds certainly aren't good. Nine out of ten start-up airlines fail within the first few years, and low-fare competition is much more fierce and widespread today than 15 years ago when People Express was launched.

Hambrecht vows that Vanguard won't be making the same mistakes as People, which expanded too quickly. He says the airline will stick to its knitting—low-fare, mostly short-haul flying in areas abandoned by some of the larger carriers. Its eight leased jets ply low-traffic routes such as Kansas City to Denver, where Continental Airlines Inc. closed its hub in 1994, and Dallas to Wichita, where American Airlines Inc. recently replaced its jet service with smaller, turboprop aircraft. "We end up doing things others don't find as attractive," says McAdoo, who believes Vanguard could expand to 35 or 40 airplanes in the next several years.

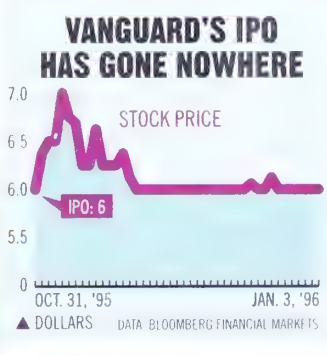
But so far, Vanguard has been doing more retreating than expanding. Only three months after starting nonstop service from Kansas City to Milwaukee, Vanguard pulled out, citing inadequate traffic. Dallas-Kansas City looked terrific until American met its fares. Minneapolis-Kansas City looked promising—until Northwest Airlines Inc. fought back. Again, Vanguard retreated.

McAdoo says Vanguard's changing route map is a sign of flexibility, not overambition. He is still pushing Vanguard into new markets, recently launching nonstop service from Kansas City to San Francisco, which is projected to bring in $20 million in revenues this year. "It's not worth spending our equity to compete with someone who can lose more in a day than the entire value of our airline," says McAdoo. But Michael J. Boyd, president of Aviation Systems Research Corp. in Golden, Colo., says Vanguard's rapid shifts show the airline isn't doing a good job of identifying opportunities. "They've been bouncing in and out of markets like a yo-yo," says Boyd.

The next 12 months will be critical to Vanguard's survival. The airline's $13 million equity cushion is dwindling. Vanguard had accumulated losses of about $10 million through the end of the third quarter, on revenue of $25.5 million, and was projected to lose another $2 million in the fourth quarter. But Hambrecht says the losses were anticipated and the worst is over. "We think they're going to make money in 1996. And assuming we don't buy a bunch of airlines, there should be plenty of cash." Still, any economic downturn or hike in fuel prices could easily defeat that rosy prognosis. Michael Lowry, president of AirWatch Report, a credit advisory service in the airline industry, says that although Vanguard isn't in immediate financial danger, it must start showing profits by the end of September if it is to survive next winter, the industry's slowest season.

But investors hoping to get in on the next ValuJet Airlines Inc., whose shares quintupled during 1995, are growing restless. Vanguard's stock price chart resembles the Denver airport—sharp peaks and then a flat, dull runway. The compa-

HAMBRECHT: *A costly flight of fancy?*



ny's shares, after an initial runup, have stayed virtually flat after an initial flurry following its Oct. 31 ipo. At $6 a share, the company has a market capitalization of about $55 million. By contrast, when Western Pacific Airlines, a Colorado carrier, went public in December, its stock price rose from $19 a share to $25, giving it a peak market cap of about $250 million. "I'm miffed the market hasn't identified Vanguard's potential," says Cameron Burr, who bought shares along with his father Donald C. Burr, the driving force behind the creation of People Express. Don Burr, who is retired and not involved with Vanguard's management, declined to be interviewed.

Some insiders say McAdoo's fierce aversion to spending, learned the hard way at People Express, may be holding back the airline. Vanguard certainly isn't throwing any money around at its cramped corporate headquarters, which is lodged on the mezzanine level of the Kansas City International Airport terminal where restaurants once were.

At least McAdoo's biggest shareholder says he's happy so far. Hambrecht, whose investor group controls 50% of Vanguard, says things are going so well that he's even looking at investing in one or two other airlines, possibly in Europe or elsewhere outside the U.S. But as his People Express experience has taught him, starting up an airline is a bit like piloting an aircraft: an aircraft whose wings have a way of coming off.

By Susan Chandler in Kansas City, Mo.

REAL ESTATE

MR. HOLIDAY INN HE AIN'T

Will Middle America check into Ian Schrager's hip hotels?

New York hotelier Ian Schrager is living proof that when you move in the right circles, a checkered financial past need not stand in the way of a bright, star-studded future.

A former co-owner of Studio 54, the defunct nightclub that symbolized the excesses of the 1970s, the 49-year-old Schrager served time for income-tax evasion and later developed, with various partners, three trendy luxury hotels in New York. More recently, he bought one in Miami and another in Los Angeles. Tapping Schrager's Studio 54-era connections with the rich and famous, his hotels have catered to celebrities and wannabes in the media and entertainment worlds. Those connections also have helped finance new ventures; Madonna is a business partner in the restaurant at the 238-room Delano in Miami Beach, his newest hotel, which opened last June.

Although Schrager's major New York projects have spent time in bankruptcy or defaulted on loans, that has not stopped the charismatic, soft-spoken entrepreneur from attracting high-powered investors such as Apollo Advisors LP, headed by Leon D. Black, and Amstar Group Ltd., a Denver-based real estate investment concern.

And in a bid to build a national network of stylish boutique hotels, Schrager is eyeing his biggest deal yet—a joint venture that could involve as many as 20 hotels in New York, Atlanta, Seattle, and smaller cities. He's mum on details, but industry sources say Schrager is talking with Starwood Lodging Trust, a real estate investment trust with interests in 48 hotels, including the 652-room Doral Inn in New York. Starwood CEO Barry S. Sternlicht declined to comment. Schrager admits the deal would test whether his hotels' trademark avant-garde style can gain broad acceptance. "This is put-up-or-shut-up time," he says.

SCHRAGER: *"This is put-up-or-shut-up time"*

Indeed, industry experts remain skeptical that these kinds of hotels will make money in mainstream America. If it comes off, his new venture also will test whether Schrager can lay to rest a reputation for overborrowing, financial wheeling and dealing, and hardball tactics. Schrager shows investors "great projections—and then finances to the hilt," says one former associate. Investors "like riding on his PR." For his part, Schrager says "the businesses were always successful, but they were overleveraged." He also attributes the hotels' earlier financial difficulties to the recession and the downturn in the New York real estate market; his hotels, he says, now generate $120 million in annual revenue and operate in the black.

Expanding his empire will require Schrager to give up some duties to professional managers and resist his stubborn—and costly—urge to fuss over every design feature, from toilet paper holders to mirrors. To bolster his operation, Schrager recently hired experienced top executives from the Omni Hotels and Marriott International Inc. hotel chains. The new hires have installed centralized reservation and purchasing systems. Another thing going for him now is timing: Experts forecast record profits for the industry in 1996.

Schrager actually got his start as a lawyer in the 1970s representing college buddy Steve Rubell's steak-house chain. Together, they launched the Studio 54 nightclub in 1977 and became deities of the disco set. But the Internal Revenue Service crashed the party by discovering sacks of unreported cash. Convicted for evading $800,000 in taxes, Rubell and Schrager received 3½-year jail sentences, reduced to 20 months after they fingered other club operators.

After prison, they pooled their remaining $60,000 in 1982 and approached New York real estate investor Philip Pilevsky to arrange $6.1 million in financing to buy a seedy, 154-room hotel they renamed the Morgans. Pilevsky took a 50% interest and Schrager and Rubell split the rest. After two years and $4 million in renovations, the Mor-

On his financing problems, Schrager says: "I made a mistake, and I didn't say no to the money"

gans opened in October, 1984, and soon posted occupancy rates of more than 85%. The partners' friendships with such entertainment figures as Bianca Jagger and David Geffen added cachet.

That celebrity aura, former associates say, also helped lure lenders. In 1987, at the peak of the real estate boom, Schrager and Rubell opened their second New York hotel, the Royalton, a pricey establishment with surreal, avant-garde design and $230 average room rates. A year later, the Bank of Tokyo Ltd. extended a $46 million refinancing on the hotel, and in 1989, it refinanced the Morgans for $30 million.

Then came a string of misfortunes and troubled deals. Rubell died of hepatitis in July, 1989. The recession took its toll. The Paramount Hotel, which Schrager opened in August, 1990, siphoned guests from his other hotels. The Morgans filed for bankruptcy protection in 1991, and the Royalton filed three years later. Meanwhile, a partnership involving Schrager defaulted on a $3.5 million loan secured by the Paramount.

Other deals failed. Plans to convert the Barbizon Hotel into an urban spa sputtered when renovation financing didn't materialize, and lenders, including the Bank of Tokyo, foreclosed on the property in 1993. Nonetheless, the partnership of Pilevsky, Schrager, and real estate developer Arthur Cohen still managed to extract a hefty fee for arranging a sale to a third party.

SELF-RELIANCE. But Schrager's deft maneuvering left lenders, contractors, and other creditors holding the bag. With the backing of Amstar Group, Schrager bought back the Morgans in October, 1994, for $12 million and spent an additional $1.6 million on renovations. Now he's planning to buy the Royalton out of bankruptcy.

Moreover, some vendors claim that Schrager clips them on bills. "It was always a nightmare getting paid," says one frustrated Morgans creditor "We watch every penny and fight for every penny," Schrager concedes. By late December, subcontractors had slapped about $400,000 in liens against the Delano, although they are now being satisfied. For a renovation this complex, $400,000 in liens isn't much, says Schrager.

In part, Schrager blames his troubled track record on easy money. "It was a feeding frenzy among the banks—everyone wanted to get into hotels—and I wasn't smart, and I made a mistake, and I didn't say no to the money."

Now, even though banks are cautiously making hotel loans again, Schrager says he's relying more on equity investors—including himself. For example, of the total $26 million cost of buying and renovating the Delano, only $14 million is borrowed. The rest is equity, primarily from the Apollo Group.

Apollo and Amstar, Schrager's new partners, "drive harder deals than the real estate guys," he says. Amstar CEO David B. Agnew says that after investing in the Morgans and monitoring the Delano, he concluded that the boutique concept could be expanded to other cities and invested in the $17.4 million acquisition of Mondrian Hotel in Los Angeles, now undergoing renovation. "One thing certain about Ian is that he brings a special niche to the hospitality industry," Agnew says. Maybe. But how profitable that niche will prove in the long term is questionable.

By Gail DeGeorge in Miami, with Phillip L. Zweig in New York

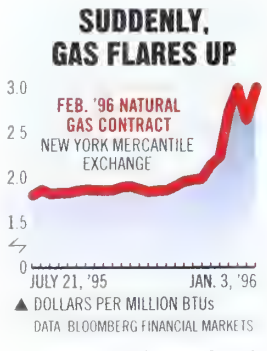
COMMODITIES

A HOT ITEM CALLED HEAT

Icy weather is stoking the price of natural-gas futures

Chicago steelmaker A. Finkl & Sons Co. could fuel its 35 blast furnaces with oil or electricity instead of the natural gas it now burns. Yet even as gas prices spiked up during the past two months, President Bruce Liimatainen has been sitting tight. "It's a short-term blip in the market," he says.

But what a blip: Futures prices doubled in the last six months of 1995, to $2.62 per million BTUs, including a 29% gain in December alone (chart). The contract for January delivery at the New York Mercantile Exchange shot up 15% in a day, when it expired on Dec. 21. A week later, prices for February delivery took off, closing at $2.99 per million BTUs on Jan. 3, up 14% in two trading sessions.



MERCURIAL. What's happening? Colder-than-normal weather, especially in the Midwest and the East, the nation's top gas-consuming regions. Heating requirements ran as much as 13% above normal in November and December—and gas suppliers were caught unprepared for the sudden surge in demand.

But the hot market in gas is not just a matter of mercury. The rally's seeds were planted last year, when many utilities and industrial users switched to gas from more expensive fuels to take advantage of prices that were about half today's. Usage soared 7.8% in the second quarter and 10.4% in the third. That limited suppliers' ability to salt away gas for winter.

When the cold weather came early, suppliers rushed to buy, paying a premium for gas that could be delivered quickly. With everyone chasing the same quarry, cash prices for gas soared in the Eastern half of the country—the weather in the West remained mild—and that pushed up futures prices on the New York Mercantile Exchange, the nation's principal market for natural-gas futures.

But at least two factors should put a damper on natural-gas prices. New York Merc officials have tripled the amount of margin money needed to trade futures—a move that tends to cool speculation. Perhaps more significant: Meteorologist Joe Davis of Smith Barney Inc. predicts the nation's coldest air will shift westward, which would reduce heating demand on the populous East Coast.

For Liimatainen of Finkl steel, there are some monetary costs as well as the management time and trouble associated with switching fuels. And those are costs users don't want to incur if they think gas prices will flag soon. "It does not take much," he explains, to send prices down—or up—as the market knows all too well.

By Greg Burns in Chicago

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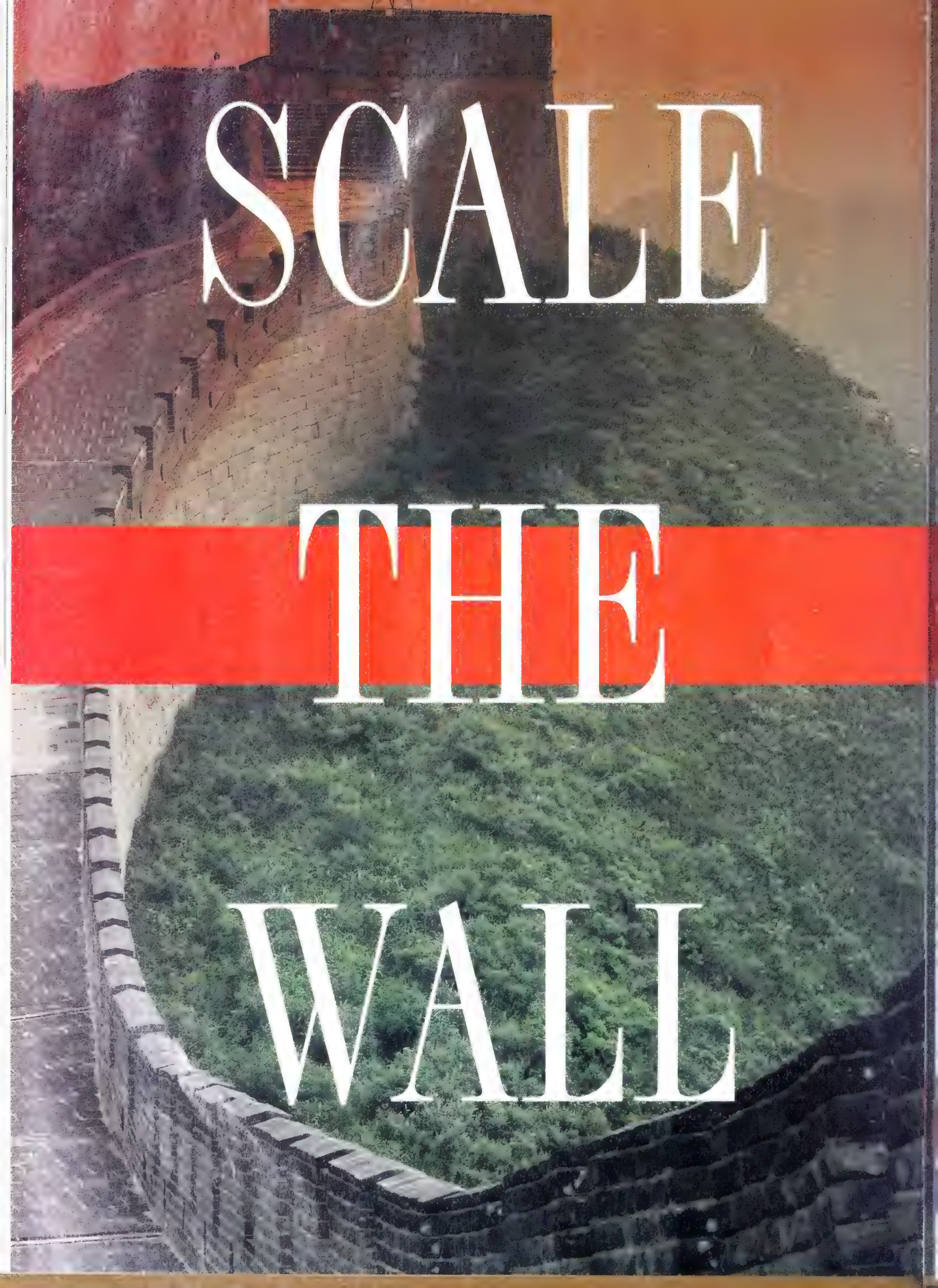
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BY GENE G. MARCIAL

LUMEX IS ALL SET TO GET IN SHAPE

The Street can be stubbornly unforgiving when its expectations are dashed. But that can produce some alluring bargains, says Michael Connor, managing partner at CB Partners, a New York hedge fund.

Take Lumex (LUM), a leader in health-care and fitness equipment. In spite of the robust performance of the Dow, the stock is trading near its lows, at around 9 a share—down from more than 15 early in 1995. Why? Investors

DATA: BLOOMBERG FINANCIAL MARKETS, CB PARTNERS

were disappointed that Lumex didn't sell one of its two major businesses some time ago to boost its stock.

Well, the new management that took over in September announced in mid-December that it would at last sell a unit, also called Lumex, that makes health-care equipment, including wheelchairs and specialty seating, and would focus energies on its Cybex division. But that still hasn't lifted the Lumex share price.

"Investors continue to ignore the stock," notes Connor. It trades below the book value of $11.58 a share. Partly for that reason, he and other pros are convinced that Lumex is a bargain.

"The stock is washed out because investors don't care—after two years of disappointments," says Connor. But he believes the shares are undervalued and are worth 20, judging from Lumex' assets and earning power.

The Lumex division alone could fetch $8 a share, based on recent sales of similar outfits, figures Connor. He expects proceeds would be distributed among shareholders. The unit posted revenues of $61 million in 1994 and an estimated $65 million in 1995. The sale of Lumex and the accompanying restructuring are expected to produce a loss for 1995 and in the first half of the new year. But Connor expects earnings of 40¢ a share for all of 1996, mainly because the company will concentrate in bolstering the Cybex unit, which makes rehabilitation equipment. Its products are sold to physical-therapy clinics, hospitals, rehab centers, and other fitness facilities.

"Cybex will be a big winner as a stand-alone company," says one investment manager who also has been buying shares. Cybex, which produced revenues of $70.4 million in 1994 and an estimated $77 million in 1995, is expected to post $90 million in 1996 and $105 million in 1997, he says. Connor notes that no analysts cover Lumex now. "But they will soon wake up to the new Lumex."

IS SOMEONE OUT TO DEVOUR SMITH'S?

Just as the drugstores are consolidating, grocery chains are teaming up, too. Competition in the industry is intense, notes an analyst, and profit margins slim. A perfect setup for mergers and acquisitions?

"You bet," says a strategist at a New York investment bank who has been buying into Smith's Food & Drug Centers (SFD), trading on the Big Board at 26 a share, near its high of 27¾—after drooping to 18 in August. This pro is convinced that Smith's, a Salt Lake City chain with 145 outlets in eight Western states, is a takeover target. He believes American Stores (ASC), also based in Salt Lake City, which operates 1,600 food-and-drug stores in 27 states, has its eye on Smith's.

"The strategic and geographic fit is there for an American Stores-Smith's Food link," says the investment strategist. He thinks Smith's large food-and-drug centers appeal to American Stores, which owns such food operations as Lucky Stores in California and Jewel-Osco in New Mexico. Its drug outlets include Osco Drug in Illinois and Sav-On Drugs in California.

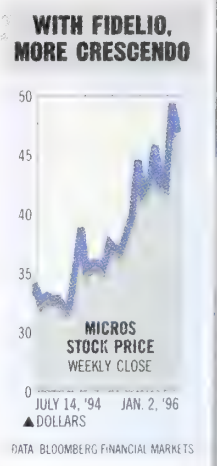
"Rather than open up new units, American Stores is thinking of acquiring established chains" that offer both food and drug products, says one analyst, whose securities firm does business with American Stores. In a buyout, this analyst thinks Smith's Food is worth 40. American Stores declined comment. Smith's didn't return calls.

WHY THIS TECH STOCK DIDN'T TANK

Technology stocks were stunning performers in 1995, many of them hitting lofty peaks—before later slumping, giving back much of their gains. But not all headed south: Little-known MICROS Systems (MCRS), for instance, whose stock was trading at 27 a share in mid-May, zoomed to 49¾ at the end of December, pulling back on Jan. 2 to 47.

Not bad for an outfit that doesn't make very sophisticated gear. MICROS makes custom point-of-sale electronic terminals for hotels and restaurants, including fast-food and institutional food-service eateries. The systems help clients improve efficiency, customer service, and inventory control. Westinghouse owned 62% of MICROS but sold its stake this past summer.

MICROS' earnings have grown fast, notes money manager Robin Kerr of Axe-Houghton Associates, an investment firm in Rye Brook, N. Y. She believes such growth will accelerate because of its November acquisition of Fidelio Software. That buy prompted her to raise her estimates for the year ending June 30, 1996, to $1.85 a share, up from a previous $1.75. More important, she upped her fiscal 1997 number to $2.60 from $2.44. "Nobody paid much attention to this deal, but it will score big for MICROS," says Kerr.



DATA: BLOOMBERG FINANCIAL MARKETS

Fidelio was a great bargain, at a price of $35.4 million, she says. A fast-growing player in systems for property management and central reservations, it posted 1994 revenues of $36 million and an estimated $57 million in 1995, says Kerr. For 1996, she foresees Fidelio revenues of $70 million.

Analyst Bill Loomis of Ferris Baker Watts agrees. "Fidelio is growing rapidly and capturing market share," he says. Based on MICROS' own growth plus the addition of Fidelio, Kerr figures the shares are worth 65.

The 1995 Business Week Europe Forum of

Financial Directors

The Right Hon. Douglas Hurd addresses European financial directors at the Business Week Forum

"Product cycles are immeasurably shorter. Price pressure is incessant."

George Cox
chief executive, Unisys
Gt. Britain & Ireland

The New Competitive Realities

The changed world business scene dominated discussion at The Business Week Europe Forum of Financial Directors. "We operate in markets that are being reshaped," said **George Cox**, chief executive of Unisys in the United Kingdom and Ireland. "We still compete on product, price, and quality, but look just beneath the surface. Product cycles are immeasurably shorter. Price pressure is incessant. Quality is no differentiator when everyone has it. We compete on the same things but it is difficult to get a permanent edge.

"What matters is how quickly you can get new products out — repeatedly — while competing constantly on product, price, and quality, while continuously moving forward, and while endlessly countering the opposition. Systems, processes, structure, and culture are the four enabling factors critical to that level of performance. If you get these things right, you permanently compete. If you get them wrong, the business fails."

Do I Do That?

The job of the finance director is moving through a personal restructuring equal in degree to corporate change.

"We are looking for a statesman," says **Brian Birkenhead**, new chairman of The 100 Group of Finance Directors, and group FD of Britain's National Power PLC. "The finance director's role is decisive, reporting to investors, bankers, agencies, and the public. You've got to satisfy the money markets and to do that, you've got to have a reputation. Contrast that with the scene 20 years ago when the FD would have been little more than the keeper of the keys to the safe, and would have been relied upon for a cautious, possibly even negative approach to business. Now the FD is expected to be proactive, with radical finance solutions to add to competitive advantage."

"The finance director's role is decisive. We are looking for a statesman."

Brian Birkenhead
group finance director,
National Power PLC

By Scott Shuster, consultant to Business Week Executive Programs, and chair of The 1995 Business Week Europe Forum of Financial Directors.

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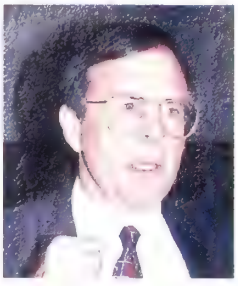

"Change has to be radical. If you stay in your comfort zone, you will not be internationally competitive."

Eric A. Croson
vice-president & managing director, Thomas Group Europe GmbH

"Transformation has to be in the leader's heart, in your heart, and in the hearts of all the senior people."

Joseph V. Marulli
president, information services, eunetcom

Radicals!

"Radical" is not the word most people in business would apply to their financial director. But radical transformation is what most companies need — and that requires a radical FD. Here are the comments of a few stand-out radicals at the *Business Week* London gathering:

Richard H. deMoll

vice-president, operation services, The Dun & Bradstreet Corporation

"The fastest way to get results is to align strategy and culture. Our chairman wanted to reduce layers and loosen up the culture. The alignment study revealed that our real estate — our office space — was a barrier to cultural change, so we tackled real estate first.

"Real estate traditionally has an 8 to 10 year payback. We decided to get that down to four years. Today I can tell you we are averaging about two years. We have reduced our real estate portfolio globally by 17 percent while at the same time dramatically enabling the rest of the transformative process. That's alignment."

Eric A. Croson

vice-president & managing director, Thomas Group Europe, GmbH

"Change has to be radical. If you stay in your comfort zone, you will not be internationally competitive because there are companies out there doing things you are not even dreaming about. For example, many of the leading Japanese firms have plans in place ensuring that their next products will be able to compete at 65 yen to the dollar. They are also cutting their product development cycle times by factors of over 50 percent. This is happening right now. That is why you, too, must think radically.

"And you must think 'fast.' Speed is the biggest competitive issue. Your reengineering efforts may be excellent, but if it's not coupled with speed, you lose.

"Also, you must use and measure *drivers.* One of the traps that finance professionals fall into is to look at ROI, profits, cash flow, and similar measures, and be driven by those results. That is the wrong approach. Results must be driven, not awaited. You must identify the drivers and then drive them. To say 'sales is our driver' is not enough and may actually be wrong. In most companies, the drivers are processes — processes with cycle times. This morning we heard British Aerospace finance director Richard Lapthorne describe how he shrank his new product development cycle time in half. That means British Aerospace can grow the top line when the competition cannot. That's the real goal."

Joseph V. Marulli

president, information services, eunetcom

"Transformation should be accomplished as quickly as possible. In a large organization, it is very difficult to change a lot of behaviors just a little bit. So if you are not radical in reshaping your focus, you will not get a substantive change in behavior. The primary determinant of how fast a transformative goal can be accomplished is the degree of commitment from the top. The chief executive's support is the sine qua non of the entire process. Transformation has to be in the leader's heart, in your heart, and in the hearts of all the other senior people."

Alain Rousset

chief financial officer, Young & Rubicam Europe

"Let me expand on what Joseph Marulli of eunetcom just said about top management support. This process can take three years, it can take four years, it can take five years. Throughout the process, the top management support Joe referred to must remain constant.

"Very often companies start to speak about reengineering because it is the fashion of the day, and then for about six months there is activity: committees and groups and so forth. Then for some reason top management focus shifts and the transformation fails. The focus has to remain very intense. The maintenance of that focus is the job that the top management must pursue most relentlessly. Without constant, full-time support from the top, reengineering becomes just a word."

Roelof R. Hendriks

chief financial officer, Royal Van Ommeren N.V.

"We changed from a company with 13 business units to one that does only three things. Our total number of employees dropped from 8,000 to 3,000, our turnover decreased from $1.25 billion to $625 million — and our profitability increased from $18.75 million to a forecast $43.75 million.

"Our debt equity ratio improved more than 100 percent and our market capitalization more than doubled.

"We started by considering procedures, systems, core activities where we would earn most of our money in the future, determining which companies had to be divested and which to be grown. But more important was that we set about creating a new spirit. It all has to do with people, so culture and mentality are essential factors."

Two Very Unusual Bankers

When *Business Week* invited **The Right Honorable Douglas Hurd** and **Peter D. Sutherland** to address our Europe Forum of Financial Directors. Mr. Hurd was UK Foreign Secretary and Mr. Sutherland was Director-General of the GATT, now the World Trade Organization. By the date of the conference, both had left government and both had become leaders of investment banking companies.

"The world is full of politicians who talk about finance without knowing anything about it, and financiers who talk about politics without having the first idea about the political scene," said Hurd. "We live in a world where politicians need to be elected and the business community needs an understanding of that. But equally, politicians have to understand that their bread and butter depends on the success of business. Politicians and business leaders actually need to live in each others pockets, for their own good. The temptation to be scornful of one another is deeply misguided." Hurd delivered a ringing endorsement of European integration and a single currency, warning that "the debate on this subject has belonged to the political chatterers. The next leap forward should be a single currency, an economic union. But this measure, designed to be unifying, has so far had the opposite effect. If this persists it may cast into doubt what Europe has already achieved. And what we have achieved is very notable. The progress against any background of history has been stupendous, and we really must not proceed in a way that causes the

The 1995 Business Week Europe Forum of Financial Directors

The Right Honorable Douglas Hurd

Give Us A Government That "Gives A Little Push"

Companies in transformation need all the help they can get, and financial directors at The Business Week Europe Forum were vocal in expressing disappointment at government services.

"Government needs to understand that there's a real world out here, and that a little push here and there makes all the difference."

Richard Lapthorn
finance director,
British Aerospace

"I am jealous of the Americans," said **Richard Lapthorne**, finance director of defense giant British Aerospace. "We are fighting on our own here in the UK. Government needs to understand that there's a real world out here, and that a little push here and there makes all the difference."

Governments the world over are in competition to position themselves as best-places-to-do business. "We were humbled recently by the news that Ohio was the only American state to be named as having one of the ten best economic development agencies in the world," said **Donald E. Jakeway**, director of the Ohio Department of Development. "We see economic development as a business: serving the site selection needs of enterprises. As Joseph Marulli of eunetcom pointed out a few minutes ago, achievement does not happen by accident. We study the needs of foreign and domestic corporations, and design and implement the financial and other incentives required. When we have to, we pass new laws. Governor Voinovich involves himself personally."

"We see economic development as a strategy to create win-win relationships."

Donald E. Jakeway
director, Ohio
Department
of Development

Ohio's statistics are astounding: more new facilities and expansions than the combined total of 28 states and the District of Columbia; more manufacturing companies selling "value added" products in the world market than any other state. Ohio's record of success is so impressive other states benchmark their economic development efforts against Ohio.

Because of his success rebuilding what *Governing Magazine* called "one of the more decayed buckles in the Rust Belt," Governor Voinovich has been named by *Governing* as the "Governor of the Year."

Ohio is ending the century as it began - as America's economic development leader.

Ohio
America's Economic Development Leader

Peter D. Sutherland

"The use of derivatives by some to gamble and take risks rather than to hedge risk has complicated the task of financial oversight."

Professor Richard C. Marston
James R.F. Guy professor of finance and economics; director, Weiss Center for International Financial Research, The Wharton School of The University of Pennsylvania

single market to unravel."

"We must address," said Peter D. Sutherland, "whether we have an institutional structure that allows us to move into the next millennium without catastrophe. After World War II, the free world created new structures for this purpose. Today it has become a little unpopular to speak positively of some of those forms of cooperation. But these are among the most noble ideas that mankind has ever conceived: movements to bury historic hatreds, and challenge xenophobia, nationalism, and racism. Today, politicians have again discovered that people can easily be persuaded by protectionist rubbish. Protectionism is a seductive argument, but it is one that the corporate community should work to defeat."

Derivatives: Not A Gamble (Unless, Of Course, You Choose To Gamble...)

As governments worry about a few high-profile disasters, financial directors feel constrained to restrict the use of derivatives. FDs themselves are not afraid of derivative instruments; the problem they face is justifying the use of derivatives to directors and other corporate constituents who have been spooked by bad news.

"The disasters had a sobering effect. But derivatives still offer an excellent way to transfer risk."

Hans-Peter Bauer
head of global derivatives, Union Bank of Switzerland

"The market has a memory, but it tends to be fairly short," says **Hans Peter Bauer**, head of global derivatives for Union Bank of Switzerland (UBS). "The disasters had a sobering effect. After a period when many shy away, the rest will see the success of the most prudent users of these tools — the vast majority — and will realize anew that derivatives offer an excellent way to transfer risk."

Professor Richard C. Marston, James R.F. Guy professor of finance and economics, and director of the Weiss Center for International Financial Research at The Wharton School of the University of Pennsylvania, notes that "The wide array of derivatives enhances the ability of firms to reduce their financial risk, but also provides opportunities to take new risk through placing complex bets on market movements. And this has complicated the task of overseeing financial activities within firms."

Dr. Marston's Weiss Center co-sponsored a survey of derivatives use among non-financial firms in the US, discovering that just over 40 percent of the manufacturers and other firms that employ derivative products do so at least occasionally to "take a view" — to place a bet on the direction of interest rates or other factors.

UBS's Bauer emphasized that derivatives make it possible for "someone to hedge a risk and someone else to take a risk. That is what we are doing at UBS; we are shifting risks around. The process is complex, but the purpose is quite straightforward, widely understood, and widely utilized on a global basis, in spite of recent questions. I hope that people will not have to learn again the hard way that if they leave their positions open in a gamble, they can lose. Derivatives should be used carefully, but not to use them at all would just be the next big mistake — like the stock market fool who sells at the low, and buys at the high."

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COMPUTERS

SAVIOR FROM DOWN UNDER?

Aussie Ian Diery's plan for AST: Get PCs to market faster

For most personal computer makers, it has been another bountiful holiday season. Not for struggling AST Research Inc. and its new CEO, Ian Diery, though. This season, Diery was focusing on survival. His goal: Apply the brakes on AST's yearlong free fall and start mapping a recovery plan.

Diery, former executive vice-president of Apple Computer Inc., was named president and CEO of AST on Nov. 2, replacing founder Safi U. Qureshey, who remains as chairman. Within days, the 46-year-old executive had sketched out a turnaround plan to restore AST to its former glory. Its key points: be first to market with leading-edge products, coddle resellers so they prefer dealing with AST rather than Compaq or Hewlett-Packard, and get better at figuring out where the PC market is headed.

Can it work? It is, after all, the same strategy that helped AST grow into a $2.5 billion company. But somewhere along the way, about the time of its ill-fated $112 million acquisition of Tandy Corp.'s computer operations two years ago, AST lost direction. Since then, it has been plagued with endless reorganizations and revolving-door management. It hasn't posted a profit since March, 1994. Sales growth has been anemic, despite an industry boom, and the company has piled up $205 million in losses (chart). For the quarter just ended, Salomon Brothers Inc. analyst John C. Dean estimates that AST will post a $38.2 million loss on revenue of $616.5 million.

OUTSOURCING. Things hit bottom last fall. For the quarter ended Sept. 30, AST's revenues plunged nearly 20% from the same period the year before, to $403 million, and the company reported a $96 million loss. That was enough to drop AST, once the fourth-ranked PC maker, to 10th place for the year, according to market researcher International Data Corp. IDC estimates that in 1995 the company sold just 566,000 computers in the U.S., down more than 20% from 1994. With a horrendous product mix—the company had no low-end home PCs and was slow to market powerful high-end models—the 16-year-old veteran of past PC wars was displaced by companies such as Hewlett-Packard Co. and Digital Equipment Corp. that weren't even in the market two years ago.

PLAY BALL: *Diery possesses a rugby player's pugnacity*

The market rout has sent AST running back to Korea's Samsung Electronics Co. for help. Samsung, which acquired a 40% stake in AST in August for $378 million, on Dec. 21 agreed to guarantee AST a $200 million bank credit line and extend $100 million in credit for component purchases. In exchange, it gets options for 4.4 million shares that will bring its ownership up to 45%. More important, AST will let Samsung name another director, ceding it majority control of the board.

How to put AST back in the fast-changing PC game? Diery's first proclamation: Being first is more important than being best. In other words, even if AST's in-house engineers think they have a new twist on PC technology, Diery won't even consider building that into a new model if it means coming out late. After all, AST's problems started because it kept missing product-launch dates as engineers fiddled with features. As late as a year ago, it was designing everything from motherboards to keyboard-controller chips by itself. Rivals such as Packard Bell Electronics Inc. that bought such components were able to come out with new machines based on the latest Intel chips much sooner. "Now, we have to focus on what we should do ourselves and what we should outsource," says Qureshey.

FAST PROFIT. That extends all the way to the very guts of the computer. Diery is now ready to start buying motherboards from Intel—as most rivals already do. "At the moment, we're months behind delivering higher-speed systems," he says. "We're going to Intel—they do a fabulous job, and we should take advantage of it." With product development cycles as short as six to nine months, Diery says all the money must be made in the first four months in order to break even on a new product.

He's also putting AST back into mass-market consumer stores with a new line of home PCs. Concluding that most home PCs were unprofitable, the company had killed off the low end of its AST Advantage! brand last year—with dire consequences. Stores started dropping AST's single remaining home computer in favor of HP, which fielded a full line under its new Pavilion brand. Even Radio Shack, once a sure outlet because of the three-year supply agreement that came with the Tandy buyout, in August started

> Diery is returning to the home PC market that AST had nearly abandoned

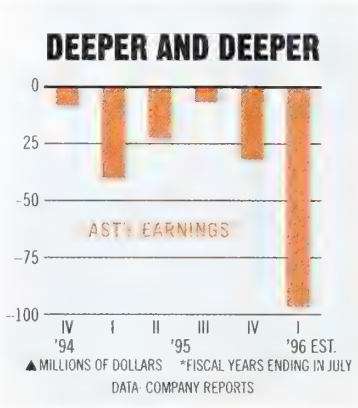
featuring IBM's Aptiva computers in the ads for its 6,600 stores.

Now, Diery is reviving the company's home PC line and expanding the number of models to match rivals, though he missed the hot holiday selling season. "You can make money there if you have a well-balanced product line," he says.

"FUNDAMENTALS." The only way to get back in the game with companies such as Compaq and Packard Bell is to read the market minute by minute, says Diery. So the hyperactive Australian is demanding a more market-focused approach around AST's Irvine (Calif.) headquarters. The new boss is trying to make the company's sprawling operations—with plants in Texas, Ireland, Hong Kong, Taiwan, and China—more responsive to changing preferences among buyers. He demands that reports on each day's bookings and billings around the world be on his desk by 10:30 the next morning. "This business is all about trends," he says. "We've got to get the fundamentals in place."

Diery has shown he already knows how to read a trend. He built Apple into the No. 1 U.S. brand in Japan with such marketing tricks as sponsoring Janet Jackson concerts. Later, as executive vice-president, Diery was instrumental in pushing multimedia to make the Macintosh a popular home PC. But he was forced out of that job in April in a restructuring orchestrated by Apple CEO Michael H. Spindler.

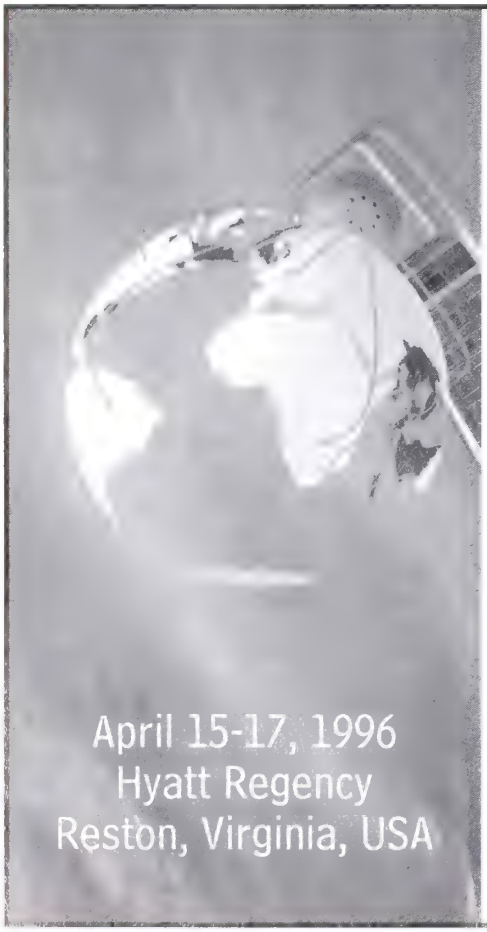
Diery, who was regarded as a bit abrasive in Apple's consensus-driven culture, didn't follow the typical career path to the top. He's a gregarious amateur rugby player and competitive horseman. After dropping out of college and trying his hand at a number of small businesses, including one to sell color TVs, he backpacked through Asia and Europe, doing odd jobs to pay his way. In 1977, he found himself driving a cab in London and yearning for a real job. So he called IBM, Xerox, and Wang Laboratories for interviews but skipped the first two when Wang hired him on the spot to sell word-processing systems. He rose quickly at Wang, eventually heading up the company's European unit, and then worldwide operations.



Turning AST around, though, is going to take more than super salesmanship. "There's no question that hiring him is a great start," says analyst Kimball H. Brown at Dataquest Inc. "But AST has been skimping on management for too long." Diery will have to move fast to refill the executive suite. In September Qureshey fired President James T. Schraith and two managers. Three other executives have since left.

Despite AST's troubles, no one is willing to write it off. "The PC industry is full of companies who hit the wall and came bounding back," says Lise J. Buyer, technology analyst at T. Rowe Price in Baltimore. If AST does come back, Diery stands to make out on the deal. In addition to a base salary of $700,000, he has options for 1 million shares he can start to exercise once the stock—hovering around $8.50—hits $9.37. That should give this salesman incentive to make his quota.

By Larry Armstrong in Irvine, Calif.



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MEDICINE

BOB GALLO'S NEW WEAPON AGAINST AIDS

A discovery of HIV-fighting natural chemicals–and a new institute–return him to the research forefront

Just a few years ago, Dr. Robert C. Gallo's life was "worse than a series of Kafka nightmares," he recalls. The National Institutes of Health and the feared Energy & Commerce Committee bloodhounds of Representative John D. Dingell (D-Mich.) were investigating the prominent National Cancer Institute scientist for possible misconduct. The charge: that the fiercely competitive, hot-tempered Gallo had grabbed too much credit for the discovery of the AIDS virus—perhaps even stealing HIV itself from French rivals.

His well-funded lab—famous for discovering the first human tumor virus, proving that HIV causes AIDS, and developing a blood test for the disease—was virtually paralyzed. "Depending on the time of day, I felt either like the Angel Gabriel or Lucifer," he says.

COLORFUL CAREER. Now, the 58-year-old virologist is definitely back on the side of the angels. The NIH probe never found any wrongdoing and the congressional investigation ended after last year's Republican victory. "We never did get to the truth," sighs former Dingell sleuth Bruce F. Chafin. Meanwhile, Gallo's colorful career is soaring again. On Dec. 19, a Maryland legislative committee approved $9 million in state money to set Gallo up as head of a new Institute of Human Virology at the University of Maryland. The same month, his lab scored another major coup in the struggle to understand AIDS—identifying long-elusive natural chemicals that cells use to suppress the virus.

"This is great for the field—and for Bob," says AIDS researcher Dr. Anthony S. Fauci, director of the National Institute of Allergy & Infectious Diseases. "In spite of the fact that the guy's been knocked around for the last five years, he's now got his own institute, and bingo, he has made a major discovery."

Gallo's rebound comes amid other encouraging news in the fight against AIDS. The past year has brought both major new knowledge about the virus and important new drugs. And the recently identified natural substances "open up a whole new avenue for thinking about how to control HIV," says Gallo. These developments, as well as progress with vaccines and other drugs in the lab, lead him to proclaim that "AIDS will be a clinically curable disease in the next 10 years."

BOLD HOPES

"AIDS will be a clinically curable disease within 10 years," Gallo proclaims

Most researchers would be reluctant to stake a claim on so difficult a foe as AIDS. But the statement is vintage Gallo. "Sticking my neck out stimulates me to do more work," he says. Others wish the virologist would think more before he opens his mouth. "My mother told me this would be my death knell if I didn't cut it out," he admits.

He never will, of course. But Gallo's 10-year prediction could be more than just hyperbole. Last January, for example, David Ho of the Aaron Diamond AIDS Research Center in New York and George Shaw of the University of Alabama proved that HIV doesn't mysteriously lie dormant in the body only to emerge years later, as once thought. Rather, the virus goes on the attack from the very start, making up to a staggering 10 billion copies a day.

Yet confronted with this pernicious assault, the immune system does manage to keep the upper hand for years—sometimes even a decade or more (illustration, page 88). Scientists now believe that dramatic gains could be made by providing the body's natural defense with a little help early on. "This is the most hopeful thing to come out in years," says Dennis M. Burton of Scripps Research Institute. "The virus is not a sinister thing waiting to hop out. Instead, it wins just by grinding you down."

Simply reducing viral levels in the body might stave off the progression to AIDS for years. The first drug approved for the disease, AZT, doesn't do the trick because the rapidly mutating virus quickly develops resistance. But since November, the Food & Drug Administration has added to doctors' arsenals by approving Glaxo Wellcome PLC's 3TC and Hoffmann-La Roche's saqui-

navir. Along with others in the development pipeline at drugmakers such as Merck & Co., these treatments are not only more potent than AZT, but in various combinations, "they work infinitely better than AZT alone," says Max Essex, chairman of Harvard University's AIDS Institute.

No one expects combinations of drugs, however promising, to be the sole answer. The virus will develop resistance, and there are major questions about long-term toxicity and cost. That's why many scientists are excited by the identification by Gallo—and by Reinhard Kurth of Germany's Paul-Ehrlich-Institut—of naturally suppressive chemicals.

As far back as the 1980s, Jay Levy, a virologist at the University of California at San Francisco, showed that certain immune-system cells—called killer T-cells, or CD8 cells—release chemicals that suppress HIV in test tubes. But many scientists discounted the finding because no one could identify the chemicals.

Until Gallo. Originally, the NCI scientist stayed out of the search. But by 1994, some of his AIDS-vaccine experiments were giving contradictory results. There was no way of explaining why some vaccinated animals were protected against the virus and others weren't. "We got tired of saying, 'Could the reason be the bloody CD8 factor?'" Gallo recalls. So when the answer didn't come from Levy or others, "I had to do it," he says.

TWO FINDINGS. Gallo's team, led by Paolo Lusso and Fiorenza Cocchi, had one big advantage. Over the years, his lab had generated a key research tool: a number of killer T-cell lines that could be grown indefinitely. Some of the cell lines produced copious amounts of natural substances for regulating the immune system. From there, it was conceptually simple, if technically challenging, to identify a cell line that suppressed the virus. Then researchers purified and identified the chemicals the cells made.

It turned out that there were three chemicals involved, and all three need to be present to suppress the virus. The substances were known "chemokines," a class of chemicals the body uses to call in immune cells. According to work by Germany's Kurth, another suppressive substance, interleukin-16, may also be involved.

These substances are unlikely to work as drugs. "We don't know how to control them, or what the side effects will be," explains Stanford University AIDS researcher Thomas C. Merigan. And Levy, for one, believes something else—still undiscovered—is the key CD8 factor. But when scientists learn exactly how the chemicals manage to block HIV in the test tube, it may be possible to develop drugs that mimic their action or boost their natural production. Gallo hints that he's close to figuring out how the chemokines work.

Having Gallo hot in pursuit of the mechanism is bad news for his competitors. Not only is Gallo likely to win, but many rivals resent the way he trashes their work in the process. "Gallo isn't the kind of person who can merely be a major player in a field, he has to monopolize it," according to one critic.

Gallo himself admits to past excesses of "vainglory" and temper. "My skin is probably way too thin for someone in the position I'm in and who exerts ego," he says. Yet his weaknesses may also be his greatest strengths. "He looks at a competitor almost like an enemy," explains one friend. "That gets him in trouble. On the other hand, that's the driving force that makes him great."

GAMBLE. Now, Gallo is bringing his determination to his new institute in Baltimore. The goal, he says, is nothing short of curing AIDS. As he sees it, the institute will be able to rush research advances into a clinical unit headed by Dr. Robert R. Redfield, former chief of retroviral research at the Army's Walter Reed Army Institute of Research in Washington. A company called Omega Biotherapies Inc. has been set up by Gallo and private investors to commercialize promising therapies.

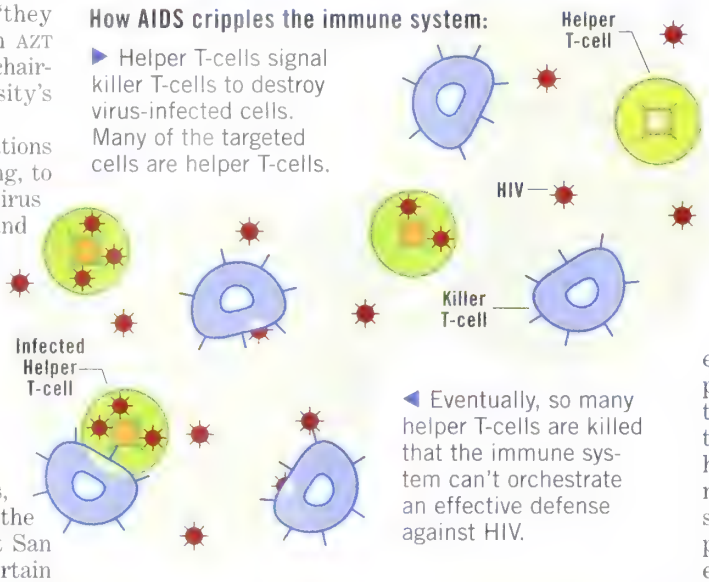
The whole enterprise is a gamble for Maryland, which outbid Virginia, Pennsylvania, and South Carolina in wooing Gallo. "It was clear that this was a man whose scientific reputation was extraordinary," says James T. Brady, Maryland's secretary of business & economic development. But with Gallo's lab making progress not just with chemokines but also hormones and vaccines for tackling AIDS and its complications, it looks like the right move. "In the area of investments that people make in scientists, I think this is as good a bet as you can get," says the NIAID's Fauci. Gallo may never live down his controversial past, but at least his Kafkaesque nightmares are over.

By John Carey in Washington

The Immune System's Surprising Weapons

How AIDS cripples the immune system:

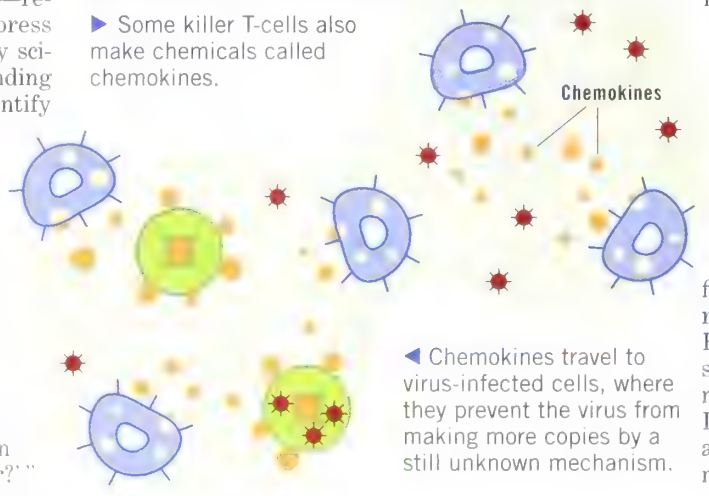
▶ Helper T-cells signal killer T-cells to destroy virus-infected cells. Many of the targeted cells are helper T-cells.



◀ Eventually, so many helper T-cells are killed that the immune system can't orchestrate an effective defense against HIV.

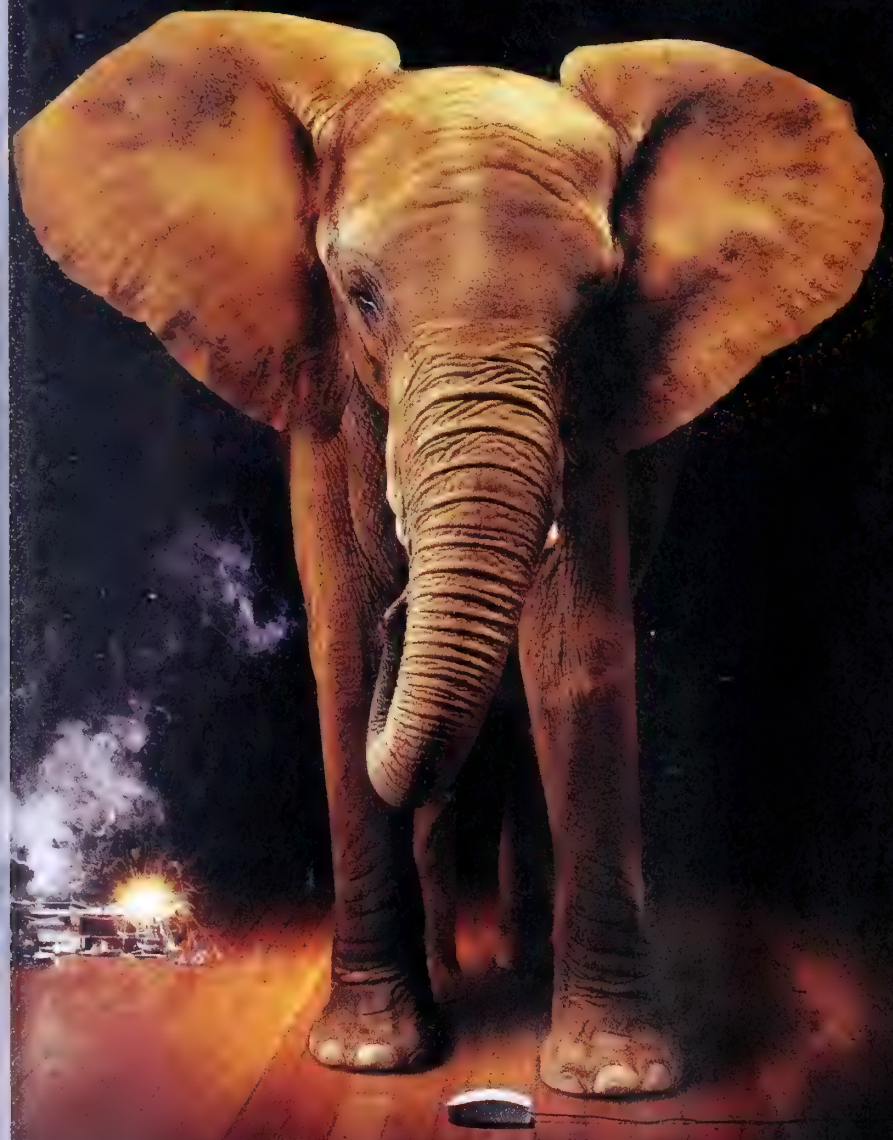
How boosting a natural defense mechanism could help:

▶ Some killer T-cells also make chemicals called chemokines.



◀ Chemokines travel to virus-infected cells, where they prevent the virus from making more copies by a still unknown mechanism.

After failing to program his VCR for the last time, Tiny welcomed the simplicity of his HP ScanJet scanner.



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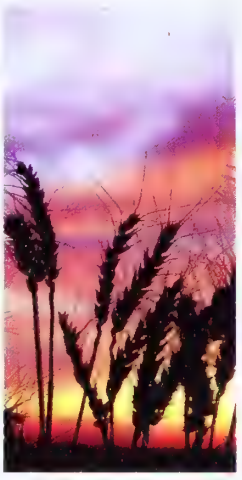


FARMERS HAVE MADE STEADY GAINS AGAINST PESTS AND DISEASES in recent years. But salty soil has proven a tougher enemy. Every year, California alone loses some $500 million in stunted crops and fields that must be abandoned because of excess salt. Now, molecular biologist Julian Schroeder of the University of California at San Diego says he has identified a gene, called HKT1, that regulates salt uptake in wheat. By manipulating the gene, scientists may be able to create salt-resistant crops.

HKT1 codes for a protein on the surface of roots that acts as a molecular highway. It lets in sodium, a key component of salt, as well as potassium, a vital nutrient. Schroeder transplanted HKT1 into yeast cells, exposed them to salt, and deftly culled resistant mutations. The mutant genes make proteins that let less sodium into the root than natural proteins do without blocking potassium. Before tackling wheat, Schroeder will work with mustard plants, which are easier to genetically engineer.

CYBERSCRIP: WHEN A PENNY IS TOO MUCH TO PAY

AS THE INTERNET GOES COMmercial, cybercapitalists are wondering how much people would be willing to ante up to visit a given site on the World Wide Web. Concluding that, in many cases, even 1¢ might be excessive, Web mavens at Digital Equipment Corp. have devised a way to mint "microcash," which would let customers pay for their Web explorations in fractions of pennies.

No money has changed hands yet. But in August, DEC filed a patent on a payment system called Millicent. Like some other digital-cash schemes, it relies on middlemen—credit-card companies or digital banks—to issue scrips worth as little as a tenth of a penny to Web-site operators each time a customer "hits" their sites.

Unlike other digital-cash ideas, however, Millicent is cost-effective at tiny increments. To keep disk storage and computational overhead to a minimum, its designers stripped away certain types of guarantees, such as privacy, or a trail of signed receipts on each purchase. But that shouldn't deter customers who simply want to click from one home page to another. Proponents point out that would-be digital thieves would need to crack the security on 10,000 or more transactions worth 0.1¢ each in order to make off with just $10. Says Mark Manasse, the inventor of Millicent: "There are easier ways to make 10 bucks."

INNOVATIONS

■ Want to keep milk from going sour in the refrigerator? Carbon dioxide may do the trick, say researchers at Cornell University. Mild carbonation, too subtle to affect the taste, would kill many of the bacteria that cause spoiling. And it wouldn't add much to the price. The biggest additional cost would be stronger milk cartons to keep in the CO_2.

■ Vicious gas attacks on Tokyo subways last year showed that nerve gas isn't just a military nightmare. The U.S. Army Edgewood Research, Development & Engineering Center (ERDEC) in Maryland says enzymes from marine microorganisms can degrade such gases into harmless compounds during an attack. The enzymes could also be used to clean up spills of certain commercial pesticides, says ERDEC scientist Joseph DeFrank.

■ Barnacles on a ship's hull can slow it down by several knots, drive up fuel costs, and cause corrosion. One solution, says Daisuke Uemura, a chemistry professor at Japan's Shizuoka University: Treat the hulls with "nitroalkanes" (combinations of nitrogen, carbon, and hydrogen) isolated from sponges found in Okinawa. The nitroalkanes should prevent the buildup of bacterial films that enable barnacles to attach themselves to the hull.

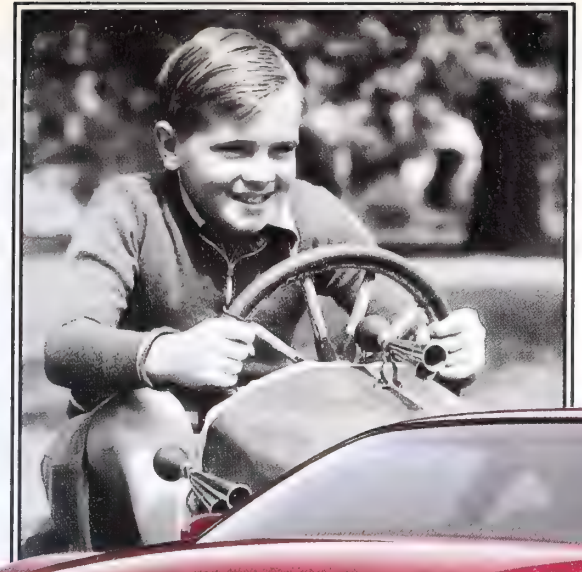
ARE BACTERIA BEHIND BLOCKED ARTERIES?

DOCTORS KNOW A LOT ABOUT risk factors for atherosclerosis—the buildup of plaques in artery walls that can block blood vessels and lead to heart attacks. Cigarette smoking, obesity, and high cholesterol levels are some major ones. But what causes plaques to accumulate in the first place? Researchers at the University of Washington say the culprit could be a common bacteria strain that most people are exposed to in childhood.

Dr. J. Thomas Grayston, a professor of epidemiology, speculates that the bacteria—*Chlamydia pneumoniae*—may either directly trigger the buildup of plaques or encourage their growth once the process starts.

In a study published in the December issue of *Circulation*, Grayston found that almost 60% of tissue samples taken from blocked carotid arteries harbored the bacteria. That doesn't prove chlamydia is responsible. But ongoing tests on mice may provide the missing evidence. If so, since chlamydia is killed by antibiotics, Grayston will propose human trials to see if such drugs can help patients with the telltale plaques.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwjan@businessweek.com



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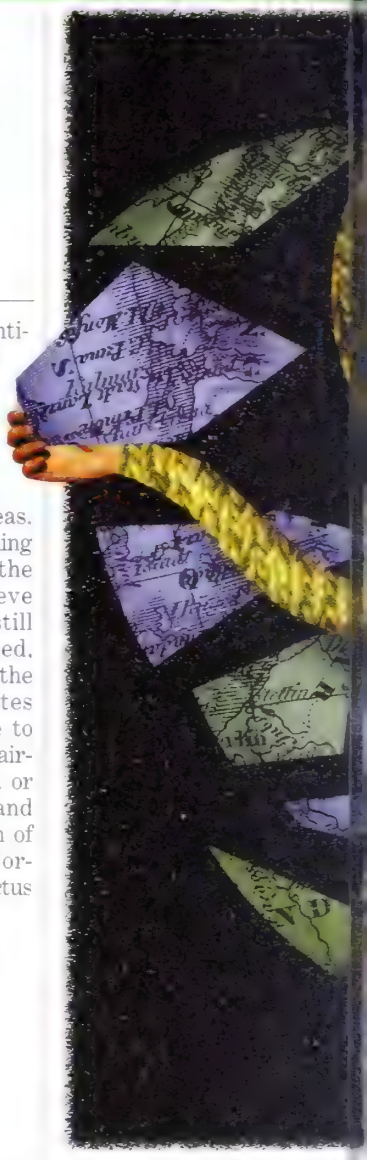
'DIVERSIFY' IS STILL THE MONEY MANAGERS' MANTRA



INVESTING After the big U.S. runup in '95, foreign markets may lead in '96

Global investors got a rude shock in 1995. The popular wisdom—that diversifying their assets around the world would maximize opportunities while reducing risk—didn't work. Instead, investors who sank all of their savings into a mutual fund indexed to the Standard & Poor's 500-stock index earned 33%, compared with an average 12.5% for sophisticates who put their money in funds composed of international stocks and bonds.

But many money managers are betting that 1995 was an exception. And the steep runup in U.S. stock prices has many investors chanting their mantra of global diversification more loudly than ever. "I think in 1996, the foreign markets will outperform, just because the U.S. did so well this year," says Sandor Cseh, chief international strategist for Boston Cos.

BONDS ABROAD. High valuations in the U.S. aren't the only reason global investors are reaffirming their multiasset philosophy. While the Federal Reserve and Bundesbank both recently lowered short-term interest rates, the Bundesbank eased more. Further reductions are anticipated elsewhere in continental Europe, Canada, and Australia, where slowing economic growth has forced central banks to rethink their tight-money policies. And the Bank of Japan continues to pump money into an economy that has been stagnant for four years. That environment bodes well not just for many non-U.S. stock markets but also for overseas bond prices. "Investors are likely to find the best returns from non-U.S. bonds, especially in the European markets," says Gary Brinson, president of Brinson Partners Inc.

Indeed, some fund managers think the lower interest-rate picture for Europe merits an aggressive position in continental bonds. Take the $498 million Fremont Global Fund, which returned 19% through Dec. 28, 1995. Half of the 27% that manager Robert Haddick has designated for his global fixed-income allocation is in European government debt. He believes overseas bonds will match or beat the 29% appreciation the U.S. bond market saw last year.

But there's a big risk: A rise in the dollar could diminish the value of overseas holdings. To guard against a higher dollar in 1996, "investors need to understand that exposure to non-U.S. equities and bonds alike should be hedged," says Brinson, who manages $50 billion for institutions and mutual funds.

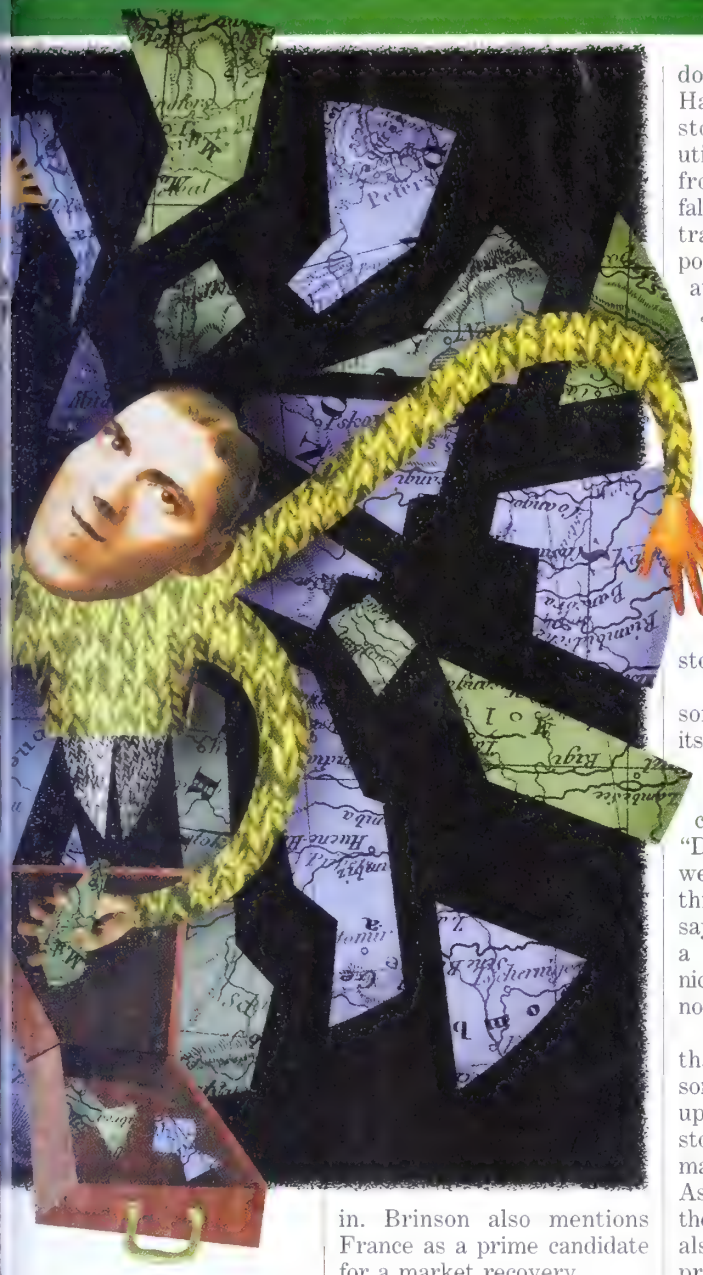
Hedging typically limits an investor's potential gains while setting a floor under possible losses. Still, Haddick estimates that 10-year government bonds from continental markets such as Germany, France, and the Netherlands should beat similar U.S. debt by at least two percentage points in the first half of 1996. On an annualized basis, he expects continental bonds to return 7% to 10%, compared with 5% to 7% in the U.S.

Some allocators are shifting their resources to capture the greater gains they expect overseas. But they are also maintaining a healthy exposure in the U.S., where many believe stock and bond prices still have room to run. Indeed, the best way to exploit the benefits of falling rates around the world may be to carve up a portfolio into fairly even slices of, say, U.S. or international stocks and bonds. That's the approach of the $895 million USAA Cornerstone Fund. Its prospectus specifies a 22% to 28% range for each asset class except gold, which is held between zero and 10%. "We're set up to stay diversified no matter what happens," says portfolio manager Harry Miller, who reviews his allocations once a quarter.

That disciplined strategy forces Miller to buy low and sell high, he says, since he must regularly replace high-flying securities that push an allocation beyond the 28% limit with less expensive ones. Cornerstone posted a 14% return for the first 11 months of 1995. For the current quarter, Miller has about 26% in U.S. stocks, where he thinks aerospace and chemicals still offer value.

Unlike Haddick, Corne-
stone's Miller had put h-
nearly 23% internation-
allocation entirely in equiti-
Now, Miller is betting a
continental bourses—mai-
ly Switzerland, Germar-
Britain, and France—whi-
he thinks will bounce as lon-
term interest rates fall. A-
he has a relatively heavy b-
on Denmark, whose fisc-
health wins his praise.

Many of Miller's counte-
parts share his enthusias-
for European stocks' attra-
tive valuations. At prices th-
average five times project-
cash flow, says Jean-Mar-
Eveillard, who runs the $
billion SoGen Internation-
Fund, "continental Europe-
half as expensive as t-



J.S." Eveillard believes that France, whose stock market was flat in 1995 amid mounting political and fiscal turmoil, represents a clear opportunity with risks already priced in. Brinson also mentions France as a prime candidate for a market recovery.

Besides Europe, asset allocators favor Southeast Asia as a region to comb for bargains. In emerging markets of the Pacific Rim, including Malaysia, Thailand, and Indonesia, Fremont Global's Haddick recommends liquid stocks such as banks and utilities. These stand to gain from lower inflation and falling interest rates and "are trading at the low to midpoint of their historical valuation ranges," he says. And John F. H. Trott, London-based chief international investment officer for Bessemer Trust Co., is putting the biggest portion of his 20% allocation of non-U. S. stocks in New Zealand and Australia. He believes industrial and banking shares there are better buys than the bigger, more commonly held resource stocks.

Trott, whose fund uses reasonable valuation as one of its stock-picking criteria, nevertheless is dedicating 45% of his portfolio to large-cap U. S. growth stocks. "Despite the rise of last year, we think there's still something more to go for," he says. Trott also recommends a sprinkling of small-cap niche stocks, with fewer technology names than in 1995.

SoGen's Eveillard agrees that the U. S. market has some buys left. He is loading up on paper and metals stocks as a play on emerging markets. He believes that as Asian economies build steam, their demand for raw materials will keep commodities prices heading upward for two to three years.

That's also why he has a relatively hefty 8% of his portfolio in gold. Explains Eveillard: "There's a supply-demand imbalance of more than 1,000 tons a year in gold," now trading at $385 to $390 an ounce. He thinks the price could go well above $500 if strong demand for jewelry continues in Southeast Asia as consumers there grow more prosperous. Besides classic mining stocks, Eveillard owns shares in Swiss-based Bank for International Settlements. A clearinghouse owned by major central banks, it has half of its assets in bullion.

TOKYO TURMOIL. Japan remains one area of disagreement among money managers. At Bessemer, Trott kept his funds completely out of the country in 1995, and for the coming year, he believes the market is still too expensive—even with the Japanese economy finally emerging from its recession.

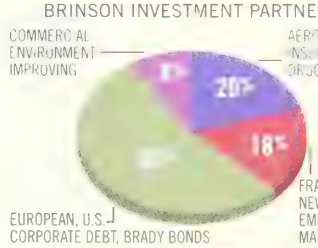
By contrast, Cornerstone's Miller thinks lower interest rates are setting the stage for better growth in 1996. And Eveillard, who bailed out of the Tokyo market before the bubble burst in '89, has started slowly rebuilding his position in Japanese stocks, which now make up 6% of his fund's total assets.

Such uncertainties, of course, are what have always made the case for diversification so compelling. The danger of a year such as 1995 is that it tends to raise investors' expectations. But history shows that whether they come from emerging markets or developed countries, 30%-plus returns rarely occur two years in a row in one place. That's why asset allocators are striving for a varied menu for '96. *Joan Warner*

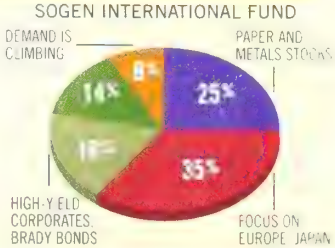
How Three Experts Will Divvy Up Their Funds

U.S. STOCKS
INT'L STOCKS
BONDS
REAL ESTATE
CASH
GOLD
U.S. SMALL-CAP STOCKS

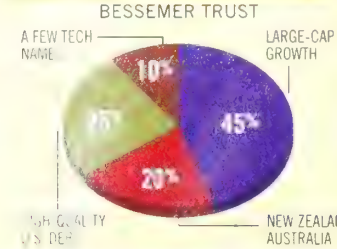
GARY BRINSON
BRINSON INVESTMENT PARTNERS



JEAN-MARIE EVEILLARD
SOGEN INTERNATIONAL FUND



JOHN TROTT
BESSEMER TRUST



DATA: BUSINESS WEEK SURVEY OF FUND MANAGERS

DAY CAMP FOR FOUR-LEGGED FRIENDS

Is Fido feeling low? Spot looking spiritless? Or, when you return from a long day at work, does stay-at-home Rover overwhelm you with rambunctiousness? If so, doggy day care may be the answer for you and your pooch.

Around the country, animal shelters and kennels are beginning to offer day care for dogs with busy owners. A few facilities even specialize in the service. "As people work longer hours, as they decide not to have children, their dogs become very important to them," says Judy Basteri of Pet Companions in Somerville, Mass. "Dogs get depressed if they're home alone 10 hours a day. They also have too much energy if they're inactive. Day care solves those problems."

"THE ANSWER." Considering that many centers call their canine clients "students" or "campers," it's no surprise that doggy day care works a lot like day care for children. Owners drop their animals off before work or the center picks them up. As soon as they arrive, the dogs start playing. They are walked regularly and perhaps receive some training or grooming if that's what their owners want. At midday, they eat the lunch their owners have prepared for them and rest for an hour or two. In the afternoon, it's more fetch, tug-of-war, and king-of-the-hill. Then, Fido goes home happy and tuckered out and ready for a quiet evening.

Once they brave chuckles from friends, many pet owners swear by doggy day care. Doug Sebesta of San Francisco spent the first year of his dog's life at home, job hunting after completing a PhD. "We bonded completely," Sebesta says of his Airedale terrier, Alex. But when Sebesta went back to work, Alex changed. He got depressed and upset every time Sebesta or his roommate even got near the front door. Finally, they decided to send Alex to the San Francisco Society for the Prevention of Cruelty to Animals' Doggy Day Care program.

"It has been the answer," Sebesta says. "He has a great time, and it relieves my mind."

Those who work with the dogs emphasize that their charges are descended from wolves and naturally feel comfortable in packs. So the day-care environment lets these dogs fulfill their need to socialize. "Most of our dogs come bounding in the door at a dead run," says Tory Weiser, director of the San Francisco SPCA program.

Facilities that specialize in day care tend to be in large metropolitan areas, such as Boston, Denver, New York, and San Francisco. But most kennels, even in smaller cities, now offer day care if requested. "Owners recognize this as a need before the kennels do," explains Jim Krack, executive director of American Boarding Kennels Assn. You can also call your local animal shelter or veterinarian for a reference.

JUNGLE GYMS. Rates range from about $10 to $30 a day, depending on the local cost of living, the level of care offered, and whether the facility specializes in day care or offers it as a sideline. At kennels, charges are usually negotiated.

Services can get quite elaborate. In Manhattan, a center called No Standing Anytime has dog runs decorated with murals and a "pet limo" that will pick up animals from their homes anywhere in the New York area. The San Francisco SPCA has jungle gyms for hyper pooches and a TV-VCR setup for dogs used to a couch-potato routine at home. In addition to day care, dogs at Cozy Inn Pet Resort & Spa in Stahlstown, Pa., may enjoy hot-oil coat treatments, Swedish massage, and swims in a bone-shaped pool.

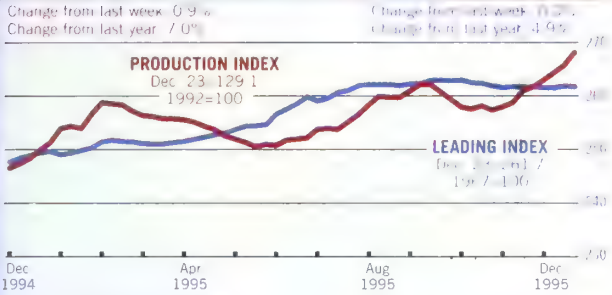
Since the idea of canine day care is just beginning to catch on, owners should be sure to check out any place they are considering for their pet and ask plenty of questions about the care given there. Does the center require that dogs are neutered or spayed and have current vaccinations? Is at least one person with the dogs at all times? Is there a provision for quiet time so that the dogs don't get overstimulated? Are animals screened so that aggressive ones aren't admitted?

Just look at your dog. Does it chew things up? Does it bark when you walk toward the door? Does it have too much energy or not enough? Has your schedule changed drastically in recent months? If the answer is yes to any of these questions, your dog may benefit from day care. And if you think that's strange, just remember that people have been sending their pets to psychiatrists and dentists for years. *Heather Mill*

After playing for hours, dogs go home tuckered out and ready for a quiet evening

Business Week Index

PRODUCTION AND LEADING INDEXES



Indexes are 4-week moving averages

The production index increased during the week ended Dec. 23. Before calculation of the four-week moving average, the index rose to 131, from 129.8 in the previous week. Seasonally adjusted output levels of autos and trucks and rail-freight traffic increased in the latest week.

The leading index was nearly unchanged in the latest week, but the unaveraged index dipped to 260.8, from 262.5. Falling stock prices and a decline in materials prices led the drop.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (12/30) thous. of net tons	1,818	1,786#	-8.8
AUTOS (12/30) units	0	138,600r#	NM
TRUCKS (12/30) units	0	[illegible]	NM
ELECTRIC POWER (12/30) millions of kilowatt-hrs	NA	63,113#	NA
CRUDE-OIL REFINING (12/30) thous. of bbl./day	NA	13,863#	NA
COAL (12/23) thous. of net tons	19,239#	19,793	-5.4
PAPERBOARD (12/23) thous. of tons	NA#	858.3r	NA
PAPER (12/23) thous. of tons	NA#	817.0r	NA
LUMBER (12/23) millions of ft.	423.0#	404.4	12.0
RAIL FREIGHT (12/23) billions of ton-miles	24.4#	24.6	3.0

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA[1], SFPA[2], Association of American Railroads

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (12/29) S&P 500	614.72	609.42	33.4
CORPORATE BOND YIELD, Aaa (12/29)	6.76%	6.87%r	-19.8
INDUSTRIAL MATERIALS PRICES (12/29)	111.4	111.4	-1.7
BUSINESS FAILURES (12/22)	NA	343r	NA
REAL ESTATE LOANS (12/20) billions	$502.3	$503.3r	8.8
MONEY SUPPLY, M2 (12/18) billions	$3,744.5	$3,736.1r	4.7
INITIAL CLAIMS, UNEMPLOYMENT (12/16) thous.	NA	341	NA

Sources: Center for International Business Cycle Research (CIBCR), Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/3) $/troy oz.	393.400	387.050	3.3
STEEL SCRAP (1/2) #1 heavy, $/ton	135.00	134.00	-6.3
COPPER (12/30) ¢/lb.	130.6	134.2	-8.3
ALUMINUM (12/30) ¢/lb	79.8	79.0	-15.1
COTTON (12/30) strict low middling 1-1/16 in. ¢/lb.	79.47	80.35	-7.9
OIL (1/2) $/bbl.	19.81	19.26	13.7

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (1/2)	6.06%	5.50%	5.98%
COMMERCIAL PAPER (1/2) 3-month	5.50	5.62	6.32
CERTIFICATES OF DEPOSIT (1/3) 3-month	5.44	5.55	6.36
FIXED MORTGAGE (12/29) 30-year	7.40	7.46	9.18
ADJUSTABLE MORTGAGE (12/29) one-year	5.63	5.60	7.38
PRIME (1/3)	8.50	8.50	8.50

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/3)	104.42	102.81	101.05
GERMAN MARK (1/3)	1.44	1.43	1.55
BRITISH POUND (1/3)	1.55	1.56	1.56
FRENCH FRANC (1/3)	4.92	4.89	5.35
ITALIAN LIRA (1/3)	1572.6	1579.5	1623.3
CANADIAN DOLLAR (1/3)	1.35	1.36	1.40
MEXICAN PESO (1/3)	7.575	7.635	5.400

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

Due to the prolonged Washington utdown, all government release data e certain to be postponed.

STALLMENT CREDIT

onday, Jan. 8, 3 p.m. ▶ Consumers prob- ly added $8.8 billion in installment cred- in November, according to the median recast of economists surveyed by MMS ternational, one of The McGraw-Hill Com- nies. Household debt exploded in 1995, th more than $100 billion in new borrow- gs. Much of that was in credit-card debt. October, debt increased $10.6 billion d credit outstanding probably hit a record gh of 18.9% of disposable income, even fore the holiday buying season.

PRODUCER PRICE INDEX

Thursday, Jan. 11, 8:30 a.m. ▶ Producer prices of finished goods likely rose by 0.4% in December, because of rising fuel prices. Excluding volatile food and energy, producer prices likely rose a smaller 0.2%. In November, total prices surged 0.5% because of a large gain in the seasonal adjusted price of new cars. Without food and energy, the increase was 0.4%.

RETAIL SALES

Friday, Jan. 12, 8:30 a.m. ▶ The MMS survey forecasts that retail sales increased by about 0.2% in December, following a 0.8% jump in November. The smaller increase is suggested by the flimsy sales reported by chain stores and lackluster buying of motor vehicles. Excluding cars, retail buying probably also rose 0.2% last month, after a 0.9% gain in November.

CONSUMER PRICE INDEX

Friday, Jan. 12, 8:30 a.m. ▶ Consumer prices likely advanced by 0.3% in December, says the MMS report. Most of the increase will be in service prices, because cold weather increased energy use. Weak retailing reports suggest that goods prices remained modest. In November, analysts were surprised when consumer prices were unchanged. Excluding food and energy, the core CPI likely rose 0.2% in December, after a 0.1% rise in November.

This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

BusinessWeek ONLINE

Sunday

Downsizing is up—more than ever. What's the cost in human terms? Is it really good for the economy? Talk to Stephen G. Harrison, head of one of the world's largest outplacement firms, and BW's John Byrne. **Jan. 7**
9 p.m. EST in the Globe

Tuesday

Ask three winners of BW education awards how they improved local high schools—with business support—and learn how to do the same in your community. **Jan. 9**
9 p.m. EST in the Coliseum

New Look

Check out BW Online's snazzy new design. It harnesses AOL's latest technology to make it even easier to find what you want online.

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

For a free trial diskette including 10 free hours on AOL, call 1-800-641-4848 and mention Business Week.

AMERICA Online

Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

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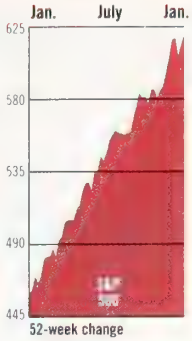
Business Week (ISSN 0007-7135) published weekly, except for one issue in January, by The McGraw-Hill Companies, Inc. Executive, Editorial, Circulation, and Advertising Offices: 1221 Avenue of the Americas, New York, N.Y. 10020. U.S. subscriber rate $49.95/year; Canada $69/year. Second-class postage paid at New York, N.Y., and at additional mailing offices. Postage paid at Montreal, P.Q. Canada Post International Publications Mail Product Sales Agreement No. 246484 **Postmaster:** Send address changes to BUSINESS WEEK. P.O. Box 430, Hightstown, N.J. 0810

Investment Figures of the Week

COMMENTARY

The stock market began the year with a bang. Blue chips advanced on Jan. 2 as investors expressed approval for belt-tightning at major companies. The Dow Jones industrial average climbed 60 points, to 5177, in the biggest one-day gain since May 31. The gain followed news of job cutbacks at AT&T and Mobil. The U.S. market continued its rally on Jan. 3, as the dollar set a four-month high against the yen. Traders were hopeful that Congress would reach an accord on the federal budget.

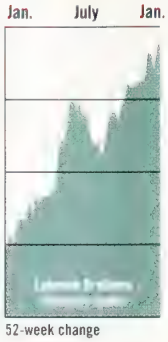
STOCKS



52-week change +34.9%

1-week change +1.1%

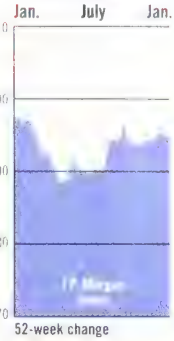
BONDS



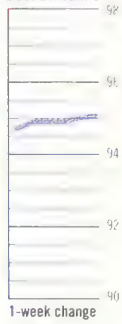
52-week change +20.8%

1-week change +0.7%

THE DOLLAR



52-week change -2.9%



1-week change +0.4%

MARKET ANALYSIS

U.S. STOCKS	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	5194.1	1.7	34.6
MIDSIZE COMPANIES (S&P MidCap Index)	218.1	0.8	29.1
SMALL COMPANIES (Russell 2000)	315.2	0.4	27.3
ALL COMPANIES (Russell 3000)	354.0	1.0	34.2

FOREIGN STOCKS	Latest	% change (local currency) Week	52-week
LONDON (FINANCIAL TIMES 100)	3715.6	1.1	21.8
TOKYO (NIKKEI INDEX)	19,868.2	-0.7	0.9
TORONTO (TSE COMPOSITE)	4819.5	2.9	16.0

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.19%	5.02%	5.84%
30-YEAR TREASURY BOND YIELD	5.95%	6.00%	7.85%
S&P 500 DIVIDEND YIELD	2.21%	2.23%	2.81%
S&P 500 PRICE/EARNINGS RATIO	17.6	17.4	17.0

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	559.9	557.5	Positive
Stocks above 200-day moving average	66.0%	63.0%r	Neutral
Speculative sentiment: Put/call ratio	0.53	0.55r	Negative
Insider sentiment: Vickers sell/buy ratio	1.29	1.24	Positive

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

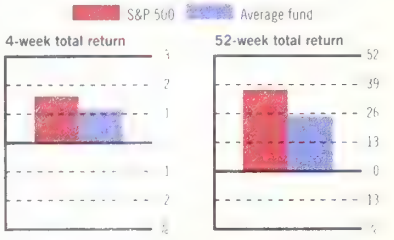
ONE-MONTH LEADERS	% change 1-month	12-month	Strongest stock in group	% change 1-month	12-month	Price
SHOES	17.3	36.3	NIKE	21.6	90.6	71 1/8
OIL AND GAS DRILLING	17.1	35.4	ROWAN	25.8	56.0	9 3/4
HEALTH-CARE SERVICES	14.3	55.7	AMGEN	17.7	97.5	58 1/4
MANUFACTURED HOUSING	12.2	40.8	FLEETWOOD ENTERPRISES	12.2	46.7	27 1/2
TOYS	9.1	39.0	MATTEL	12.4	58.0	31 3/4
ONE-MONTH LAGGARDS	**% change 1-month**	**12-month**	**Weakest stock in group**	**% change 1-month**	**12-month**	**Price**
SEMICONDUCTORS	-6.1	37.8	MICRON TECHNOLOGY	-20.2	87.5	41 3/8
PERSONAL LOANS	-4.9	45.2	BENEFICIAL	-5.9	22.4	47 3/4
COMMUNICATIONS EQUIPMENT	-3.9	52.1	ANDREW	-11.1	14.8	40
ALUMINUM	-3.7	23.8	ALCOA	-5.2	25.5	54 5/8
FOREST PRODUCTS	-2.7	10.5	JAMES RIVER	-20.7	28.5	24 3/8

MUTUAL FUNDS

MORNINGSTAR INC

LEADERS Four-week total return	%
TEMPLETON GLOBAL INFRASTRUCTURE II	12.4
EVERGREEN U.S. REAL ESTATE EQUITY Y	11.4
MEDICAL RESEARCH INVESTMENT	11.1
52-week total return	**%**
ALGER CAPITAL APPRECIATION	78.6
PERKINS OPPORTUNITY	70.3
FIDELITY SELECT ELECTRONICS	69.4

LAGGARDS Four-week total return	%
STEADMAN AMERICAN INDUSTRY	-10.1
SELIGMAN COMMUNICATIONS & INFORM. D	-8.1
MERRILL LYNCH TECHNOLOGY C	-7.5
52-week total return	**%**
EV MARATHON GREATER INDIA	-33.4
WRIGHT EQUIFUND-MEXICO	-33.4
AMERICAN HERITAGE	-30.6



RELATIVE PORTFOLIOS

DRI/McGRAW-HILL

Dollar amounts represent the present value of $10,000 invested one year ago in each portfolio

Percentages indicate five-day total returns

U.S. stocks	Treasury bonds	Foreign stocks	Money market fund	Gold
$13,874	$13,548	$12,049	$10,564	$10,186
+1.43%	+0.98%	+0.78%	+0.12%	+0.27%

All data on this page are as of market close Wednesday, Jan. 3, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close Jan. 2. Mutual fund returns are as of Dec. 29. Relative portfolios are valued as of Jan. 2. A more detailed explanation of this page is available on request. r=revised

HOW NOT TO MEASURE THE U.S. ECONOMY

When Congress and the White House finally put aside their bickering over the budget and reopen the government, one of the first things the Commerce Dept. will do is issue sweeping changes to its flagship measure of economic performance, gross domestic product. The new data attempt to give a more accurate picture of GDP, and in the new Information Age, we applaud any government effort to provide better information. Problem is, the new GDP benchmark, at least for now, lowers economic growth rates, moving us further away from the truth instead of closer to it.

Commerce's Bureau of Economic Analysis is trying to remove a long-recognized flaw in the way we compute GDP. It's something economists arcanely refer to as "substitution bias," which arises because the current fixed-weight GDP overstates the growth impact of sectors where prices are falling, such as computers. The revision, called the chain-weighted GDP, reflects price changes more quickly and continuously, lessening the influence of these rapidly expanding sectors on growth. However, the effort to eliminate that distortion is only one of many projects under way at the BEA with the intent of moving toward a better GDP measure. The correction for substitution bias, taken by itself, yields dramatically slower growth figures for recent years. For example, growth in the first three quarters of 1995, now on the books at 2.7%, drops to a meager 1.8%.

To aggravate matters, the Kansas City Federal Reserve now says the economy's new noninflationary growth limit has dropped from the generally accepted 2.5% down to only 2%. Can these numbers really be true? The world seemed dismal enough when economists calculated that the U.S. economy could grow at only 2.5% without generating inflation

Worse still, the new chain-weighted index of GDP nearly eliminates all of the previously reported strong productivity gains in the 1990s. Yet in many respects, today's economy is reminiscent of the high productivity of the 1960s, when the economy grew at a 4.4% annual rate using the chain-weighted method. Simple observation of today's low inflation, strong corporate profits, low unemployment, and nascent gains in real wages clearly indicate that productivity growth is vigorous. No wonder the latest statistics will leave policymakers and corporate chieftains more confused than ever about the real state of the economy.

The BEA is giving us only half a measure. What's still missing from a better tracking of GDP is an upward adjustment for changes in the quality of various high-tech sectors other than computers, such as telecommunications and semiconductors. Moreover, the BEA's measures of output in many service industries are still woefully inadequate. Most economists agree that modifications in these areas will push up the GDP growth rate. The BEA plans to incorporate some of these adjustments into its next GDP overhaul, which is scheduled for mid-1996. So why not wait and give us the whole pie instead of giving us a measure that eliminates one distortion while creating others?

U.S. economic data are unquestionably the best in the world, but this GDP fiasco needlessly tarnishes that hard-earned reputation. True, budget constraints have limited the ability of government statisticians to upgrade their products. Yet budget limits cannot justify poor decision-making. We all want better data, but don't jerk us around in the process.

TREAT THE NEW CHINA WITH TACT

Relations between China and the rest of the world are at a delicate phase. China is increasingly assertive, driven both by fear of post-Deng political chaos and rising economic confidence. Heavyhanded tactics surrounding the takeover of Hong Kong in 1997, Beijing's saber-rattling at Taiwan, and the sentencing of dissident Wei Jingsheng are all signs of a China determined to go its own way no matter what others think.

The temptation for U.S. policymakers is to abandon the Administration's current engagement approach, essentially separating trade from other issues dividing the two nations, and adopt policies that isolate China from the global community. Fanning American anger at China are its surging trade surplus and increasing signs that Chinese entrepreneurs can copy U.S. corporate goods and technology with impunity.

It would be far wiser for policymakers to keep to the middle ground in responding to China's emergence as a major power. In recent years, U.S. policy has vacillated between wild optimism over a market of 1.2 billion people and dour condemnation over brutal human-rights violations. Despite inevitable zigs and zags, the U.S. must somehow persuade China to shrink its trade surpluses and restrain its military might—without seeming to be unfairly trying to repress its industrial ambitions. That means engagement, not isolation.

The middle path is open. China clearly wants things from the world, such as membership in the World Trade Organization and full recognition in terms of high-level visits and hosting of international events. The U.S. should work with its allies in Europe and Asia to explain to China's leaders that there are connections between China's conduct and the world's response. China does not wish to create a united front of nations opposed to it nor to be perceived as an international outcast. Yes, condemn China on human rights, but don't go so far that the relationship is destroyed. Support Taiwan against military intimidation by Beijing, and back democracy in Hong Kong. But keep the WTO negotiations alive and maintain trade relations. No matter what, keep on talking.

AUTOS WHY THE USED-CAR DEALER IS KING

PEOPLE ▶CHRYSLER'S LUTZ ▶BofA's COULTER

DEFENSE CREATING A NEW INDUSTRY

SINESS WEEK
96 January 22

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SUN'S RISE

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Sun Microsystems to new heights.

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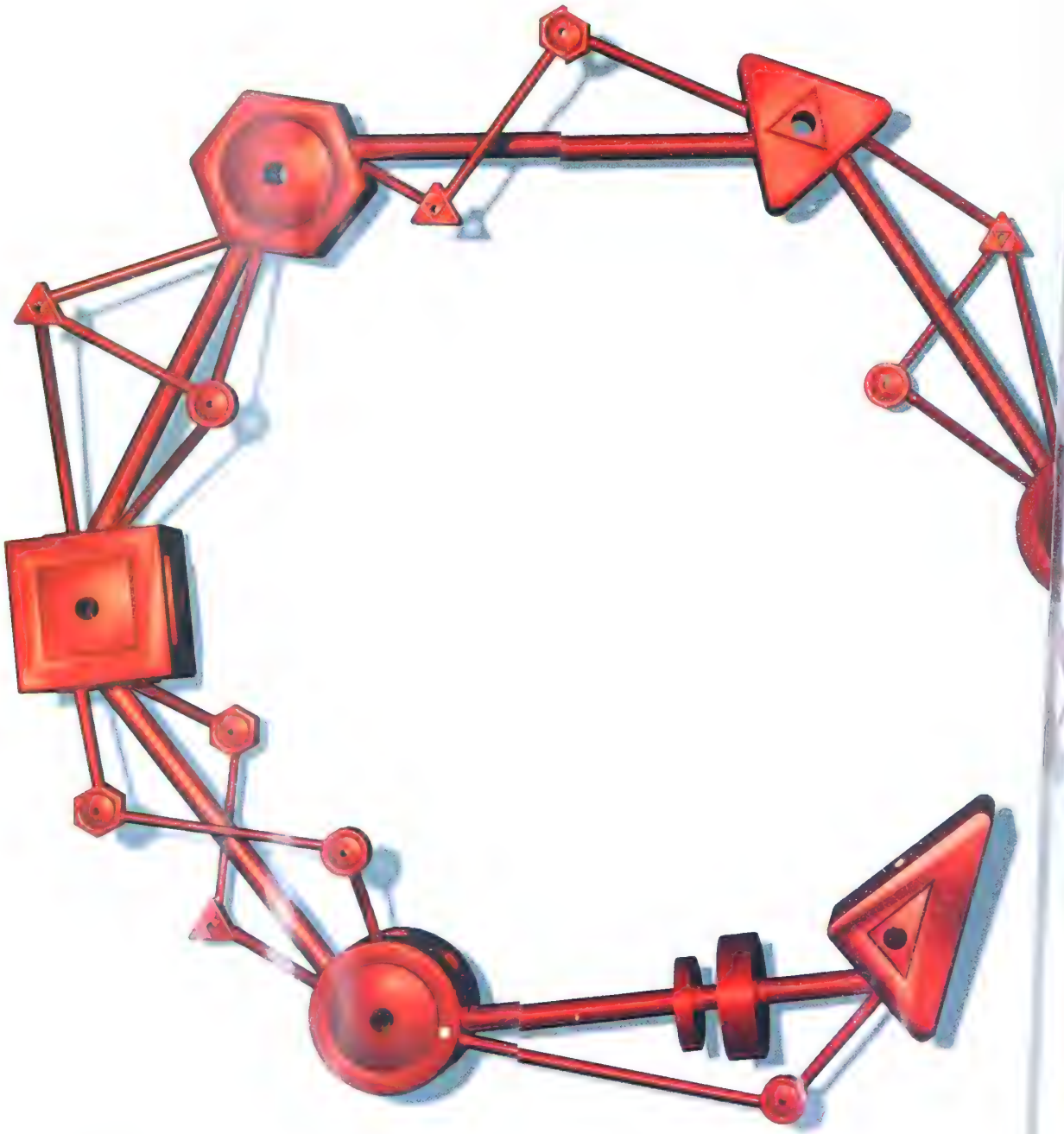
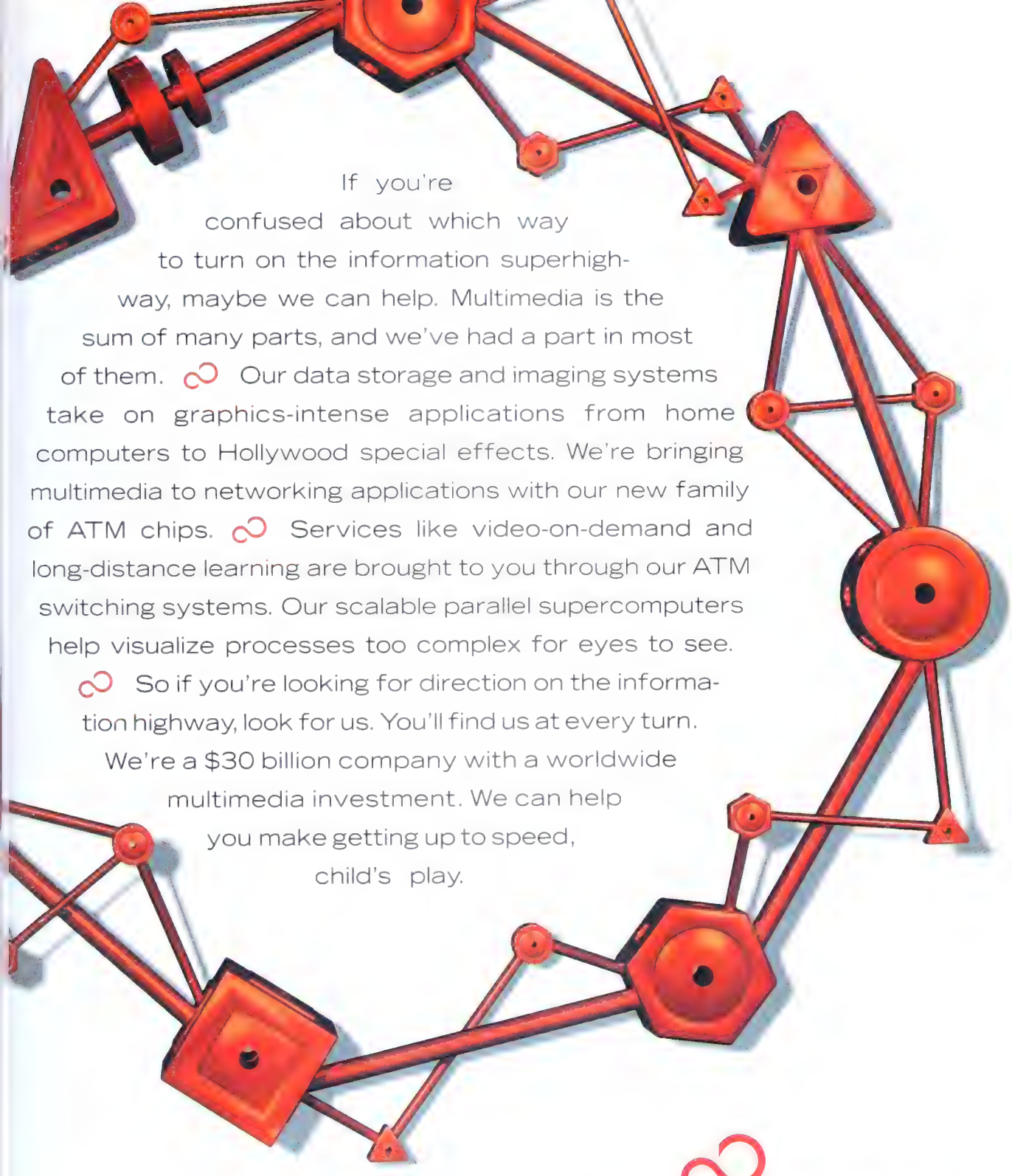
CHILD'S PLAY.





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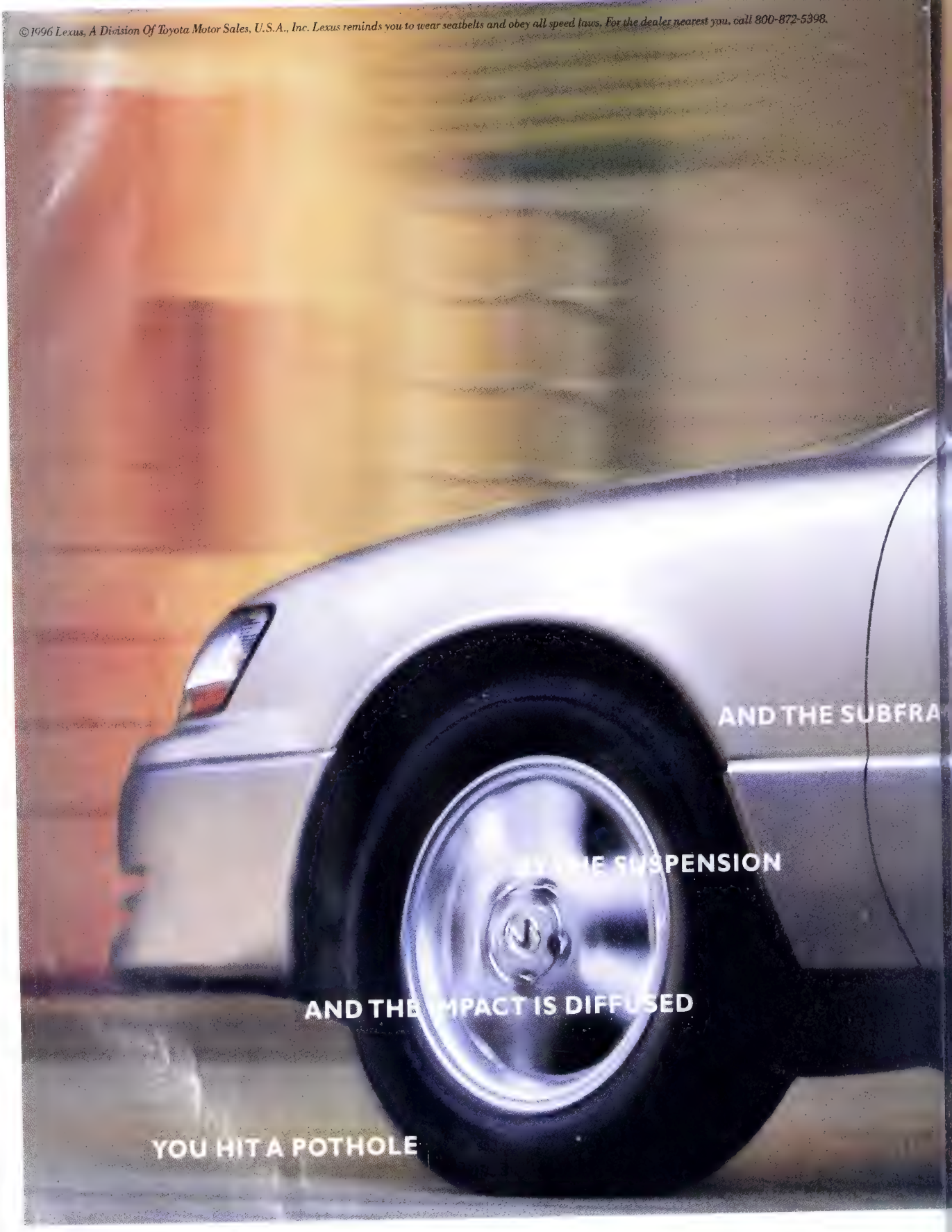

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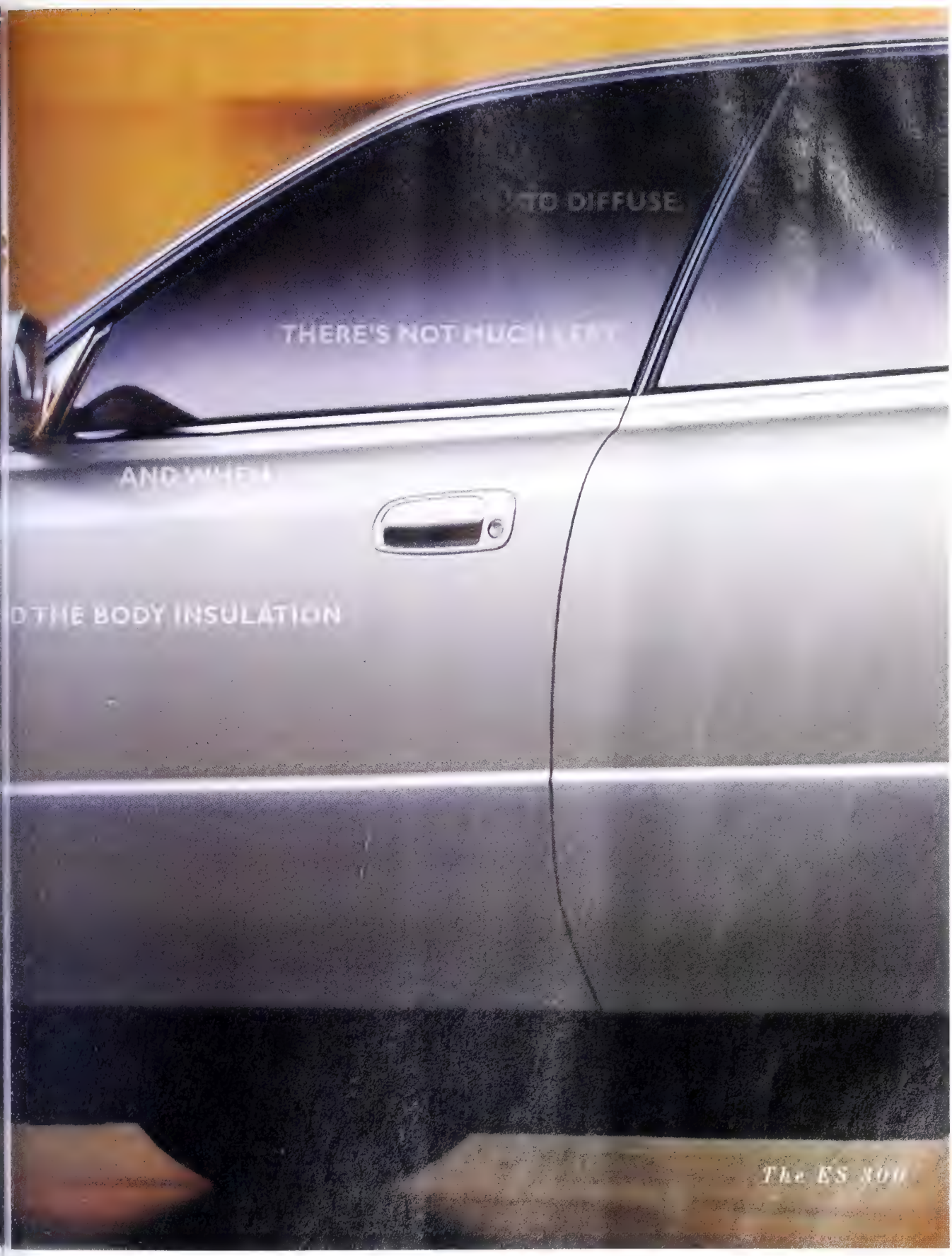

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COVER STORY

'KICK BUTT AND HAVE FUN'

How Scott McNealy has Sun Microsystems quickly moving to the center of the computing universe FROM 66

BusinessWeek

JANUARY 22, 1996

Cover Story

66 SUN'S RISE
CEO Scott McNealy's longtime zeal for network computing is finally paying off big-time. Sun Microsystems has companies from Microsoft to IBM singing its tune, thanks in part to an Internet program called Java. Now, can McNealy's passion, pranks, and financial savvy keep Sun at the zenith?

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Sun is rushing to revise its plans for the sizzling new computer language

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Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

TALK SHOW "The view of the principals in the Oval Office was that this would be a recess.... There were some people who wanted to label it a suspension."

—Clinton staff chief Leon Panetta on budget semantics

WHEELER-DEALERS

HONEY, DIDN'T WE EAT HERE IN NEW YORK?

THOMAS LEE, THE BOSTON financier with a Midas touch, is entering the ever-fickle restaurant biz. He's making a major investment in a collection of high-end New York eateries that he and fellow investors want to expand around the country and overseas. And then they plan to take the whole thing public, seeking a bonanza similar to such past Lee IPO successes as Snapple Beverage.

Lee's investment in the New York Restaurant Group, estimated at as much as $15 million, aims to bring the Manhattan Ocean Club, Park Avenue Cafe, and Smith & Wollensky steakhouse to big cities ranging from Chicago to London. The company, which will remain controlled by founder Alan Stillman, wants to open in three cities this year. The strength of Stillman's restaurant concepts, says Lee, is "they really are brands... with name recognition and consumer loyalty."

LEE: *Upscale restaurant chain*

Fine, but the casualty rate among new restaurants is notorious. Probably the only comparable chain for upscale chow that's public is the 27-outlet Ark Restaurants, owner of New York's four-star Lutèce and trendy America. Performance at Ark is spotty: In fiscal 1995, ended in September, profits dipped 2.5%, to $1.1 million.

CASINO SOCIETY

AH, A TORY LOTTERY: THE RICH GET RICHER

BRITAIN'S NATIONAL LOTTERY is a juicy issue for the Labor Party as it gears up for elections. The furor centers on the for-profit Anglo-American consortium that the ruling Conservatives chose to run the year-old game.

CHARITY? *Help feed a fat cat*

Labor MPs complain that soft regulators let Camelot Group—composed of U.S. lottery operator G-Tech Holdings and four British companies including Cadbury Schweppes—profit at the expense of funding good causes. For the six-month period ended Sept. 30, it paid almost half its $37 million in lottery earnings to Camelot owners, the legal max. Another flash point in a nation disdainful of fat paychecks is Camelot CEO Tim Holley's 1995 salary of $683,000. He declines comment.

Adding fuel to the mix: Virgin Group Chairman Richard Branson charges that Guy Snowden, G-Tech's co-chairman and a Camelot director, tried to bribe him to withdraw his 1994 bid for the lottery. Snowden denies that charge. *Julia Flynn*

PROFIT & GLOSS

GOTTA WATCH THE QUIET ONES

CALL THEM THE CORPORATE-finance booby prizes. Every year, the Association for Investment Management & Research assesses disclosure of financial and other data. The analysts' group then ranks companies against others in the same industry on a bad-to-good scale of 1 to 100.

Analysts say this year's worst discloser, Archer Daniels Midland, draws their ire because it typically releases quarterly reports long after others do. Plus, the ag products giant doesn't divulge nearly enough to satisfy them, especially seeing how it is under federal scrutiny for alleged price fixing—charges ADM denies.

ADM didn't return calls for comment, but Prudential Securities analyst John McMillin ascribes the company's arm's-length attitude to competitive pressures: It doesn't want to enlighten its many privately held rivals, such as Cargill, which don't need to disclose.

Mid-American Waste Systems objects to its low grade, saying it has improved its communications with Wall Street. But insurer CNA shrugs off its poor showing, noting that it's 84%-owned by Loews and therefore doesn't need an aggressive investor-relations effort. The top scorer: retailer Federated, at 96. *Sunita Wadekar Bhargava*

DISCLOSURE: THE LAGGARDS

COMPANY	INDUSTRY	SCORE 1 TO 100 (WORST TO BEST)
ARCHER DANIELS MIDLAND	Food, beverage, and tobacco	23
MID-AMERICAN WASTE SYSTEMS	Environmental control	33
CNA	Insurance	37

DATA: ASSOCIATION FOR INVESTMENT MANAGEMENT & RESEARCH

BROADCAST NEWS

THE FCC SMELLS A MEDIA CONSPIRACY

IT'S SWEATING TIME FOR broadcasters who have slipped around federal limits on station ownership. The Federal Communications Commission is looking to close up a loophole in the law that now forbids a company from, among other things, owning more than one station per media market or reaching more than 25% of the U.S. population. The dodge: take a minority interest in a station—and some control. That's how Rupert Murdoch built his Fox network, evading the national limits. He either owns or part-owns stations covering nearly half the U.S.

GERALDO: *point man*

Catching the attention of the FCC was a recent deal by Tribune Co., owner of 10 stations and the *Chicago Tribune*. Tribune has a 33% interest in Qwest Broadcasting which is owned by such investors as talkmeister Geraldo Rivera. Last year, Qwest purchased a pair of stations for $167 million in markets where Tribune already owns stations, Atlanta and New Orleans.

The FCC grudgingly approved the purchase, then started reviewing the ownership rules. Murdoch, Qwest and others fear they won't be grandfathered in. If the feds tighten the rules, Tribune, for instance, could be forced to sell some of its own stations or dump its stake in Qwest. *Mark Lewyn*

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Up Front

SUN BELT RISING

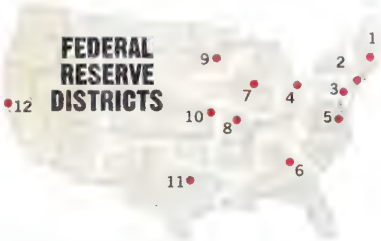
THE FED: FROZEN IN TIME

THE FEDERAL RESERVE system, created 82 years ago, has never updated the boundaries of its 12 districts. The Fed's San Francisco regional bank has 18% of the population—and many of the largest high-tech companies—while the New York regional district has just 9%.

Now, some Fed watchers think that it's time to redraw the lines, shifting banks to different cities. David Hale, chief economist for Kemper-Zurich Investments, says Congress should add another West Coast district, merge Kansas City with Minneapolis, combine Cleveland and Philadelphia, and create a Florida district. That would reflect the migration from the Rust Belt to Sun Belt, plus the shift from heavy industry to high tech.

The existing structure benefits the Chicago and Cleveland banks in particular. Their heads get special voting rights on the 19-member Federal Open Market Committee, which sets interest rates, since they're in the old industrial heartland.

Such an overhaul would have a hard time passing Congress. Regional bank chiefs are chosen by local business leaders, who wouldn't want the bank headquarters to leave. There is a recent precedent, though: The Bundesbank redrew its districts following Germany's reunification. *Dean Foust*



1 BOSTON 2 NEW YORK 3 PHILADELPHIA 4 CLEVELAND 5 RICHMOND 6 ATLANTA 7 CHICAGO 8 ST. LOUIS 9 MINNEAPOLIS 10 KANSAS CITY 11 DALLAS 12 SAN FRANCISCO

THE GOOD EARTH

FRANCE GETS RUFFLED OVER TRUFFLES

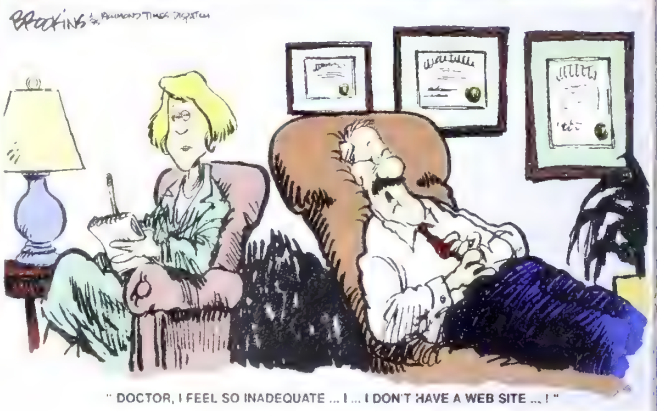
FRANCE'S TRUFFLES, SACRED to the Gallic palate, are imperiled by a two-year-old invasion from the Orient. Cheap Chinese versions of the celebrated mushroom-like delicacy are hurting French truffle producers. Average prices for French-grown truffles slumped as much as 30% in 1995, to below $400 per kilo, their lowest level this decade.

Imports of the Chinese variety, which are grown in the foothills of the Himalayas, now surpass domestic output—22 tons last year, vs. 15 tons from France. Many French farmers, fed up with the lower prices, are giving up on truffles. French production slumped 25% in 1995.

To true French truffle lovers, the biggest menace is gastronomic. They fear unscrupulous French food sellers will mix less-tasty (to them) Chinese truffles with French truffles and sell the result as the real thing. An even worse nightmare: French farmers chase higher yields by spreading the prodigious Chinese truffles around the roots of oak trees, where the fungus grows—and the Chinese hordes soon take over, spreading their inferiority. Result: calls in the National Assembly that foreign truffles be labeled. *Bill Javetski*

NOSE TEST: *Is this Chinese poseur?*

DRAWN & QUARTERED



"DOCTOR, I FEEL SO INADEQUATE ... I ... I DON'T HAVE A WEB SITE ...!"

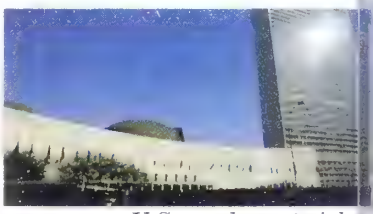
U.N. BLUES

WHO'S GETTING STIFFED HERE?

A BIG VICTIM OF UNPAID U.S. dues to the U.N. is ... Corporate America. Deadbeat members such as the U.S., the worst offender, have pushed the U.N. close to insolvency. So it is slowing payments to vendors and won't take on any new contracts other than for basic housekeeping.

Trouble is, American companies rake in a huge share of U.N. spending. The U.N. says they reaped some $737 million, or 19.5%, of the $3.8 billion total spent in 1994. One outfit getting stiffed is Price Waterhouse, on a $1.8 million computer system contract. A Price Waterhouse spokeswoman says some U.N. payments have been delayed but expresses confidence of eventually getting paid in full.

This gets worse: Several other nations, including France and New Zealand, are calling for a ban on U.N. buying from any country behind on dues. But GOP lawmakers, arguing that the U.N. is a bloated bureaucracy that smacks of world government, don't want to pay any of the roughly $1 billion Washington owes it (40% of the worldwide total)—and they plan to add $443 million to the tab this year. The White House wishes to gradually retire the old U.N. debt. *Stan Crock*



BIG BUCKS: *U.S. vendors at risk*

THE BIG PICTURE

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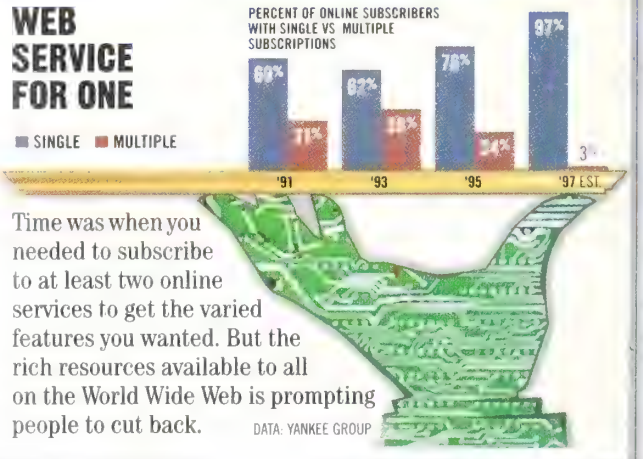

Time was when you needed to subscribe to at least two online services to get the varied features you wanted. But the rich resources available to all on the World Wide Web is prompting people to cut back.

DATA: YANKEE GROUP

FOOTNOTES Increase in Domino's pizza deliveries to Washington's essential bureaucrats for November shutdown: 68%

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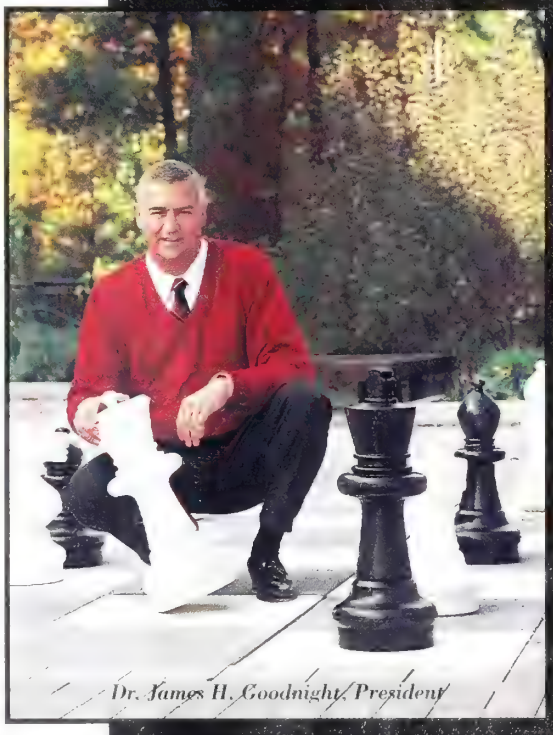

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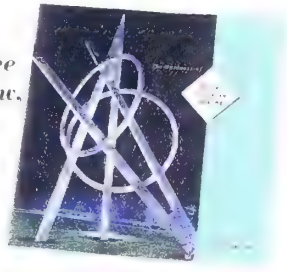

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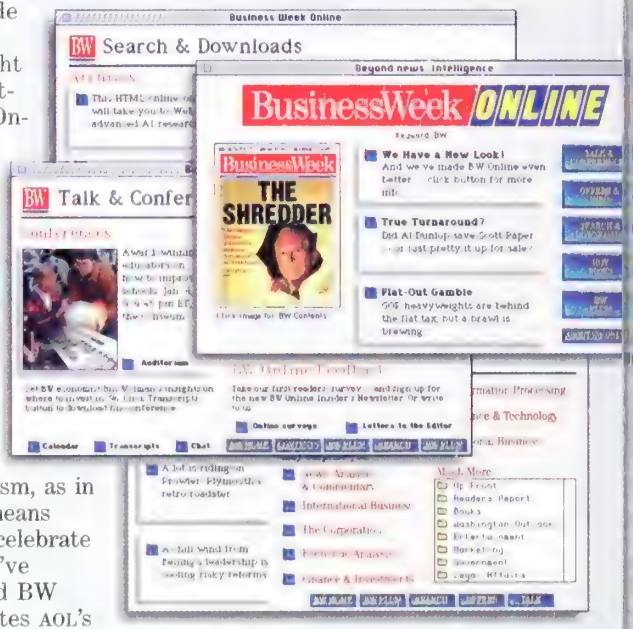
Editor's Memo

ONE YEAR ONLINE—AND GROWING

Change has always been the lifeblood of journalism—why else would the news business exist? But in 1995, the word took on a more vivid meaning: The idea of delivering visually interesting information via personal computer exploded into reality, thanks to consumer online services and the Internet's World Wide Web. A year ago, BUSINESS WEEK caught an early wave—creating BUSINESS WEEK Online for delivery over America Online, whose membership tripled in 1995, to about 4.5 million subscribers.

BUSINESS WEEK Online was an instant hit. "Someone has finally gotten it right," gushed one of hundreds of congratulatory letters. But in online journalism, as in all else, sitting still means falling behind. So to celebrate our first birthday, we've launched a redesigned BW Online that incorporates AOL's latest technological enhancements. Credit for the handsome new look goes to BUSINESS WEEK's graphics director, Arthur Eves, and the rest of our six-member online team. They collaborated with AOL producer Stephen Mobley to deliver a more versatile and easier-to-use design.

From BW Online's new screens, for example, you click just once to reach much more information. This will come in handy whether you're searching the 11,500 company listings in the BW Online/S&P Corporate Directory, sifting through our 119 live-conference transcripts (readers have downloaded 41,500 to date), looking through two years of BW archives, or perusing online-only versions of such BW features as Best Business Schools and Executive Education. Among other major improvements are numerous "hot links" that flag the day's timeliest stories and instantly take you to them. For a free AOL trial disk, call 800 641-4848, and ask for BUSINESS WEEK Online.



In 1996, we expect to make BW Online even richer and more interactive—a perfect complement to BUSINESS WEEK itself. We hope you'll sign on—and if you've already visited, come back again.

Stephen B. Shepard

Editor-in-Chief

Business Week

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JEFF VINIK'S JOB IS TO MAKE MONEY. PERIOD

In "Did Magellan manipulate the market?" (News: Analysis & Commentary, Dec. 25/Jan. 1), your reporter writes: "Prominence gives Vinik a duty to be above suspicion." Nonsense! Jeffrey N. Vinik's only duty is to make money for Fidelity Investments and for Magellan Fund's investors. If he's canny enough to fool other market players into buying while he unloads stock on them, good for him. And good for Magellan shareholders. If you want to buy a stock because Jeff Vinik has expressed an opinion, then just go ahead and buy Magellan. If, however, you prefer to go head to head with him, good luck to you!

Howard Steiner
Southport, Conn.

'BELIEVE ME, THE MIATA IS HERE TO STAY'

I had to laugh when I read "Do you have the feeling that you've been here before?" (News: Analysis & Commentary, Dec. 25/Jan. 1)—where you declare the Mazda Miata to be "out." Every year, we get some sort of pretender having a go at the most successful convertible in the world.

The BMW Z3 may be a better car (it is not), but it will never generate the kind of feelings the Mazda does. Do you really think the Z3 will have fan clubs worldwide—people running around in Z3 T-shirts or hats? Believe me, the Miata is here to stay. In 20 years time, it will be the only '90s roadster that people still talk about and drive.

Allan Elegeert
Ostend, Belgium

ETHYL CORP.: TAKING A LONG VIEW

If your analysis of Ethyl Corp.'s performance were extended to include the 1980s bull market, your findings and conclusions would be remarkably different ("This public company of ours," News: Analysis & Commentary, Dec. 11). You might be surprised to find that Ethyl outperformed even Berkshire Hathaway Inc. for most of the '80s. Challenged by the decline of a major product line late in the decade, the Gottwald family, which had pioneered the leveraged buyout, split the company into separate entities. This action was shareholder-friendly, as it allowed outside investors the opportunity to reallocate capital individually rather than as the board saw fit. The Gottwalds remain directors of the spun-off companies for an appropriate but increasingly rare reason: They are owners with economic interests in the companies. Considering the Gottwalds' investment, the director fees are irrelevant.

Accounting for all of the spin-off value created, an investment in Ethyl beginning in 1982 would have produced a return greater than twice that of the Standard & Poor's 500-stock index. This is a record that's matched by few public companies.

Sam Shapiro
Shapiro Capital Management
Atlanta

CORRECTIONS & CLARIFICATIONS

"Test-driving Java" (Technology & You, Dec. 25/Jan. 1) erred in saying that Macintosh versions of Netscape Communications Corp.'s Navigator allow people to use applications of the Java programming language. Such features are planned but are not yet ready for downloading over the Net.

"Go west, big bank" (Finance, Dec. 4) misstated a profitability target for thrifts. It is a return on equity of 15%.

THE RELIGIOUS RIGHT CAN'T SPOOK DISNEY

I was glad to see your astute analysis of the American Family Assn.-Florida Baptist Convention boycott of Disney, in response to that corporation's decision to extend insurance benefits to partners of gay and lesbian employees ("101 damnations at Disney," Up Front, Dec. 25/Jan. 1).

As strong as the voice of religious conservatism seems, it is only a very loud and annoying single-digit minority in the political and cultural panorama. Disney knows—and with this misguided boycott the rest of America will soon learn—that the religious right's actual power base isn't large enough to shave a minute off the line to Space Mountain, much less lead us into the 21st century.

Rena-paulette Guay
Madeira Beach, Fla.

HOW TO AVOID EXPLOSIONS AT AIR-BAG PLANTS

The following may provide additional enlightenment on the problems of producing air bags ("An explosive mix at TRW," Legal Affairs, Dec. 18).

There are inherent differences between Morton International Inc.'s sodium-azide manufacturing process and TRW's. Morton's process keeps the volatile chemicals essentially inert until the final stages.

Morton went through similar "incidents" (the explosive industry's term for rapid fires—known to laymen as "explosions") in the mid-to-late 1980s. As a former program manager for Morton's air-bag business with Mercedes-Benz, I can tell you that four principles guided our efforts:

1) People and safety come first. All dangerous operations should be physically isolated and controlled remotely.

2) Expect "incidents," and design for them—rather than try to create a "foolproof system." Build the system to allow for fires and prevent overpressures that do damage. In the event of an incident, all that is lost are the chemicals-in-process. You clean up and start again.

3) Maintain twice the capacity required by forecasts. It's expensive, but you will never shut down an auto assembly line.

4) Train, train, train. Any process is only as good as the people who operate it. Select the people carefully, and make them constantly aware of the hazards involved. Safety is more than design and procedures. It's attitude.

I strongly believe these principles were major contributors to Morton's excellent safety record and delivery performance. I am sure TRW has considered all of these factors as well, but if not, a word to the wise.

James M. Stone Jr.
Ogden, Utah

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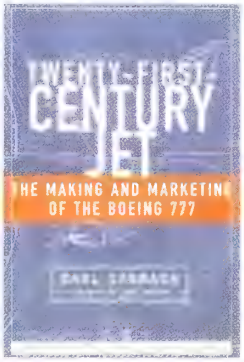
21st-CENTURY JET
The Making and Marketing of the Boeing 777
By Karl Sabbagh
Scribner • 366pp • $25

HOW BOEING HATCHED ITS HIGHEST-TECH BIRD

Boeing is not known for openness. It is remarkable, then, that half a decade ago, it decided to give British TV-documentary producer Karl Sabbagh unprecedented access to the team that designed and built its newest jumbo jet, the 777, which entered commercial service last June. Now, Sabbagh has produced a book and a Public Broadcasting Service documentary, which began airing on Jan. 8, each entitled *21st-Century Jet*. In them, he tells the story of what he calls one of the most counterintuitive of modern marvels—a 140-ton machine that appears effortlessly to defy the law of gravity.

It's an extraordinary tale, and Sabbagh, who seems to have been given the run of the production program and entrée to key figures at Boeing Co. as well as to suppliers and customers, tells it well. From the beginning, Boeing decided the 777 would be a pioneer in a number of ways. It was to be drawn up entirely on computer screens—Boeing's first paperless design. Digital data would flow directly from engineers' computers to the machine tools that cut metal. "Shims," or adjustments made to parts that don't quite fit together—inevitable on earlier jets made from paper blueprints—were to be eliminated, along with expensive rebuilding. The 777 was to be Boeing's first "fly-by-wire" plane, where electronic pulses rather than cumbersome hydraulic systems deliver pilots' commands to the actuators that move flaps, the rudder, and other control surfaces. But on the theory that it would be safer to give pilots "the ultimate authority," Boeing's fly-by-wire technology would also allow humans greater control than did the original 1988 Airbus Industrie system. That system was later implicated in at least two crashes, one of which killed 92 Indian Airlines passengers.



For the first time, Boeing would consult extensively with customers during the design phase, another innovation copied from Airbus and a distinct change from Boeing's earlier approaches. Japanese-style "design build teams" involving engineers, salespeople, and representatives of suppliers and subcontractors, as well as production staff, were to work together to produce the plane. "Working together," in fact, became the program's corny motto. It also took on an unintended irony: At the same time Boeing was

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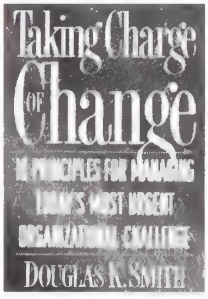

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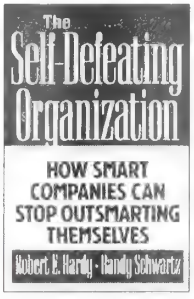

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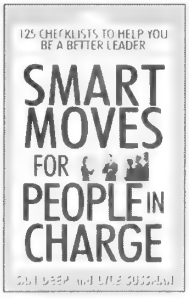

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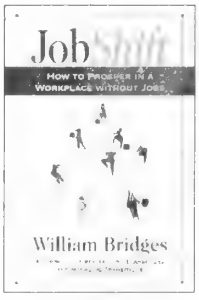

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building the 777, it was paring its Seattle-area workforce by one-third, creating anxiety among workers that was partly responsible for a strike late last year.

For Boeing executives, a key issue for the 777 was ETOPS (Extended Twin-engine Operations)—a certification provided by the Federal Aviation Administration and other regulators that the two-engine plane was safe to fly for up to three hours on only one engine—as it would have to do if an engine failed during a transoceanic flight. Early in the design phase, Boeing decided it wanted to win this certification before the 777 even entered service. This would be unprecedented: For example, Boeing's 767, also a twin-engine model, had been in operation for two years before it won its three-hour ETOPS certificate. But the credential would make the 777 a hot item in the marketplace. Here, the author provides a clear account of how Boeing employed an intense testing program—and zealous lobbying—to overcome skepticism at the FAA and elsewhere and to win the certification.

Adversity is inevitable during production of such a complex machine. Sabbagh provides several discussions of such difficulties. He describes, for example, Boeing's delicate handling of a Japanese supplier whose progress at one point was unsatisfactory and the strains on a small Australian company that managed to meet Boeing's deadlines for a rudder despite last-minute design changes.

Although all of the key players receive flattering portrayals, *21st-Century Jet* is not a puff piece. For example, Sabbagh seems to believe sincerely that safety is an overriding design consideration at Boeing. But critics of the company are given their due, and Sabbagh is mildly disapproving of Boeing executives' obvious annoyance with them. Among the critics were pilots who were skeptical of Boeing's determined drive to win the ETOPS certification. The author suggests that it was entirely understandable for "people who are not aircraft designers but who will travel in the plane...[to] seek standards of certainty about technology that are rarely achieved in any walk of life." Meanwhile, at headquarters, "the Boeing people resented this [attitude], but they really didn't know how to counter it."

With a focus on engineering and new materials, the early sections of *21st-Century Jet* will be hard going for many readers. Later, though, the pace picks up: A chapter on late-stage tests, during which a 777's tail is intentionally scraped along the runway and brakes are heated to 3,000C, is riveting stuff. "Today [test pilot John] Cashman and his crew of seven were going to sit on top of...twelve glowing brake disks until the tires deflated as the fuse plugs melted from the heat.... Might one or more [tires] explode, sending flaming shards of rubber in all directions? Might flames spread upward in some way into the landing-gear wells and thence to the plane?" Such punishing efforts go a ways toward explaining why you are far less likely to be injured on an airplane than on the drive to the airport.

BY MICHAEL J. PARKS

Parks, a BUSINESS WEEK stringer in Seattle, has been keeping tabs on Boeing for 20 years.

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BY STEPHEN H. WILDSTROM

LOG ON–AND LEARN A LANGUAGE

Speech recognition is improving, so these programs can perfect your *parlez-vous*

The computer asks for the German word for "excuse." I say "*Die Entschuldigung*" into the microphone. "*Korrekt*," responds a brisk Teutonic voice. This is not the language lab of my youth. Instead, it's *Learn to Speak German*, an imaginative, if flawed, use of speech-recognition technology.

So far, most efforts to commercialize speech recognition for personal computers have focused on letting you dictate a letter or memo to a computer, which converts your speech into text. This is an obvious use of today's technology and should cheer the hearts of the keyboard-phobic among us. But the real payoff from speech recognition may come with more creative applications, from telephone services to education.

GOOD GRADES. Language training is a natural for speech software. The $100 *Learn to Speak German* program is from Learning Co. (800 852-2255). Like its sister programs, *Learn to Speak Spanish*, *Hablemos Inglés*, and *Learn to Speak English*, it offers drills essential to language learning. While earlier multimedia language programs let you hear a foreign language, these offer instant feedback on your pronunciation as well. Not only did the program let me compare my German to that of a native in vocabulary and pronunciation drills, but a meter graded my performance from "tourist" to "native speaker." The CD-ROM program, plus a 400-page-plus workbook, are designed to cover at least a year of college-level study.

The speech recognition, built around software from Belgium's Lernout & Hauspie Speech Products, is impressive but not perfect. In the more advanced drills, *Learn to Speak German* was smart enough to recognize that there's more than one correct way to word an answer, and it accepted several variations. Yet in vocabulary drills, the program often had trouble understanding short words, such as prepositions, no matter how carefully I spoke.

Unfortunately, the program suffers from the bugginess that infects many Windows multimedia programs. I set it up on four different computers with Win 3.1 and Win95. Only one installation succeeded on the first attempt. The program crashes occasionally without warning, often producing such befuddling error messages as "Script Error. Handler not defined." A Macintosh version (included on the same CD) ran flawlessly but lacks the speech-recognition feature that makes the program so attractive.

SOFTWARE FLOOD. *Learn to Speak* wants a fast computer. Although the specs say it will run on a 33-megahertz 386DX, I found that a 90-Mhz Pentium is the slowest machine that avoids unpleasant delays while the computer analyzes your speech. A decent microphone also can greatly improve recognition accuracy. I had good results with a $30 battery-powered Koss M/21.

Language programs and dictation software from companies such as Kurzweil AI, Dragon Systems, and IBM are the leading edge of what is likely to turn into a flood of speech-enabled software. Microsoft Corp. is designing a standard way to add speech features to Windows 95 and Windows NT programs. This being the software industry, Microsoft's Speech Application Programming Interface (SAPI) effort is being challenged by the Speech Recognition Application Programming Interface Committee (SRAPI). The SRAPI group, headed by Novell Inc. and including the leading speech-recognition-technology companies, is developing its own standard for a variety of computer systems.

One hopes that some benefit will come of this alphabet soup. In the meantime, the *Learn to Speak* programs, bugs and all, are an interesting preview of things to come and a good way to learn a new language or brush up rusty skills.

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A standard computer screen is wider than it is high, but most World Wide Web pages are vertically oriented. So it helps to have a pivoting monitor, such as the MicroScan 17x from ADI Systems (408 944-

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CD-ROMS

LOOKING IT UP

Reader William S. Parker of Sacramento, Calif., is disappointed with most computerized reference works and wants an unabridged dictionary on CD-ROM. There are at least two good choices. The *Random House Unabridged Electronic Dictionary* is available for Windows at $79 (800 793-2665). Oxford University Press (800 445-9714) offers the ultimate guide to the King's English, the full *Oxford English Dictionary*, in Windows or Mac format for a kingly $895.

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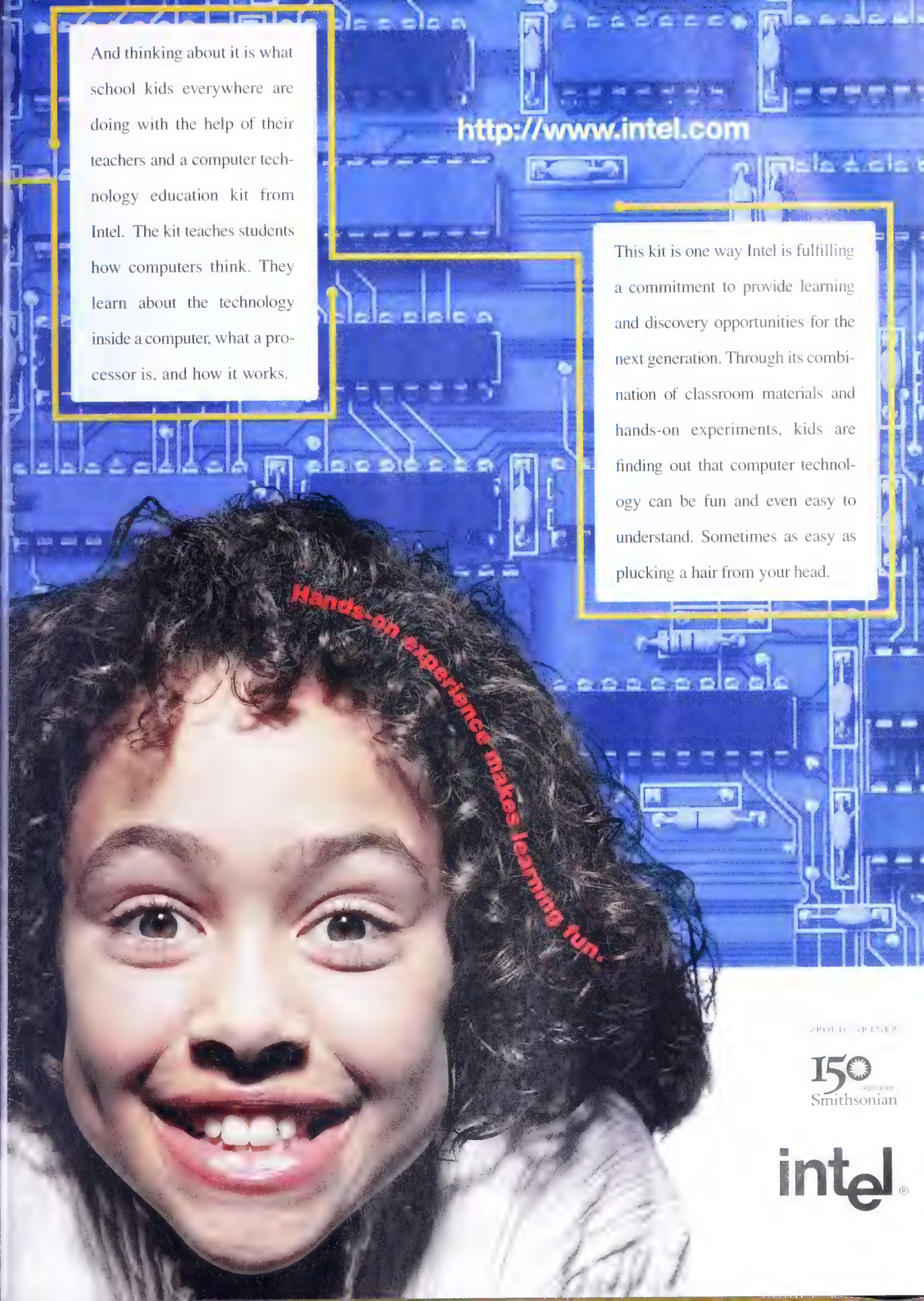
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BY RUDI DORNBUSCH

DON'T MAKE ALAN GREENSPAN A POLITICAL FOOTBALL

ACT NOW: Greenspan has done a great job, but Clinton is letting him dangle in hopes of forcing him to cut rates further

After President Clinton took office, Federal Reserve Chairman Alan Greenspan got a front row seat at the first State of the Union address, right next to the First Lady. That raised a few eyebrows. Cynics were fast to argue that the President was pampering the chairman; in an age of budget-cutting, Greenspan's monetary easing is the only path to growth. Of course, there is another view: President Clinton wanted to look financially conservative to collect a vote of confidence in the markets in the form of a drop in long-term interest rates. What better way than to have the cameras zoom in on conservatism incarnate, Alan Greenspan, smiling at the party?

Greenspan's term as Fed chairman is up in March, but the White House has been slow to discuss reappointment or succession. Capital markets take reappointment to be the only choice and view any other move as catastrophic. But if that is so obvious, why is the White House so slow to act?

In his role as chairman of the Fed since 1987, Greenspan has done an outstanding job in establishing sound money policy in the U.S. The Fed's response to the 1987 stock market crash warded off much bigger and more threatening economic fallout. Its successful slowing of the economy from 1989 through 1991 avoided a reigniting of inflation. Since then, the Fed's fine-tuning has worked wonders. The economy is at full employment, inflation is negligible, and long-term interest rates are low, almost to the point of straining belief. There has definitely been a major turnabout: Today, the U.S. is a sound money country.

WAYWARD BANKERS. Of course, there are critics. Some would like to eke out an extra 1% in economic growth just to find out exactly where inflation starts. Others would like to lower growth even further in order to push for zero inflation. Greenspan has found a pragmatic middle ground that stays away from inflation without sacrificing growth. He is short on bombastic ideology of the kind the hard-money crowd spouts, but he is long on delivering in a way the economy has not seen for three decades. Clearly, he deserves reappointment on his record alone, if only to express a firm commitment to just this kind of policy and these results.

Nobody is irreplaceable. Yet failure to reappoint would be tantamount to a wish to play with the economy, experiment, and lose. A liberal at the helm would spell a dollar collapse and a steep rise of rates. Finding the right conservative is hard. When bankers were gods, anyone might have served the role. In today's hot money world, experience on the job accounts for more than ideology. Besides, in the '90s, you can't even trust a banker to be conservative. Of course, there are always alternative candidates, but why experiment with clones if you can have the real thing?

CLOUD OF SUSPICION. The delay in reappointing Greenspan can only mean one thing: The President is trying to hold the bait, pressuring the chairman to earn his reappointment with enough interest-rate cuts to boost the economy and generate an economic boomlet in time for the 1996 Presidential election. We just had a 25-basis-point cut in rates in December; another might come in January or February. With a lag of six to twelve months, this would give a kick to the economy on election eve.

Holding out on reappointment unnecessarily politicizes monetary policy, at least in appearance. The economy at this stage, with growth slipping all over the world, requires an immediate cut in rates. If good management of monetary policy has, as a byproduct, the President's reelection, so be it. But until Greenspan is reappointed, any interest cuts create the suspicion that he is merely courting political favor. This is not the way to run policy or the economy.

The President has a responsibility to support the shift to sound money in the U.S. with a timely appointment of the next Fed chair. The appointee must obviously convey the image of continuity. Even though the appointment process is political, that should not allow it to intrude on the key consideration: Low inflation and financial stability are the top priorities.

The President should make a commitment to a speedy reappointment of Greenspan. That will do more for his reelection than the games being played now. Moreover, as the Continent messes around with a form of money, the "Euro," and as Japan flounders, the U.S. can reassert its role as the financial stronghold in the world. If the President wants to show leadership and benefit America by helping abolish a key source of macroeconomic instability, here is a good opportunity.

Rudi Dornbusch is professor of economics and management at Massachusetts Institute of Technology

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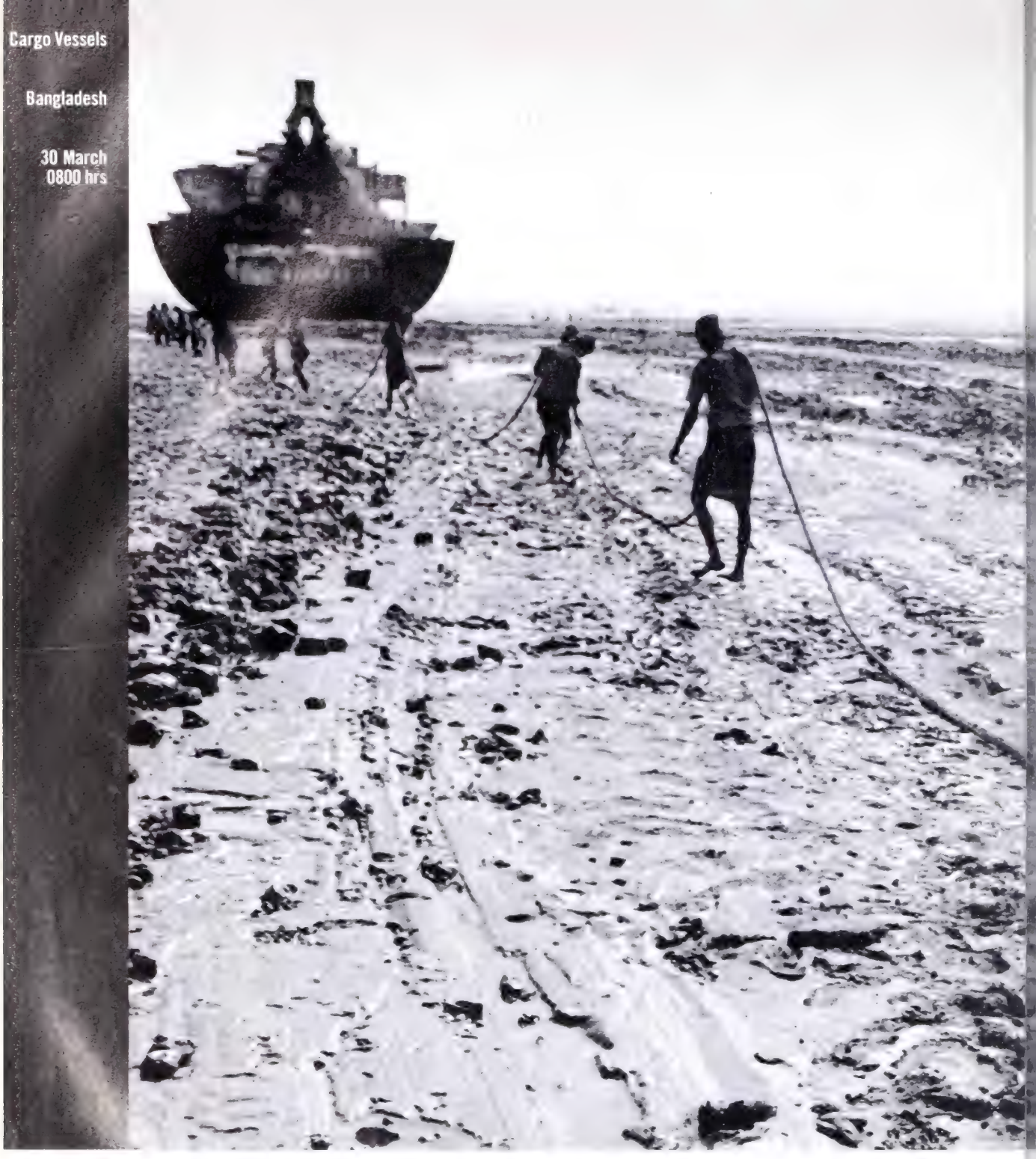

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BY GENE KORETZ

THE DOWNSIDE OF SUPPLY SIDE

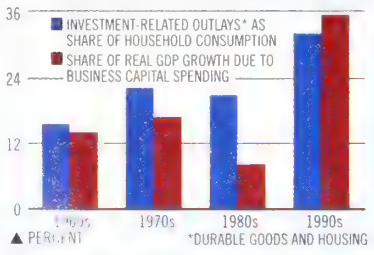
Investment has outpaced demand

A mantra of tax reformers these days is the need to stimulate greater U.S. investment and savings. At least one economist who agrees that this prescription should enhance the nation's long-term economic health, however, is deeply concerned about its possible near-term implications.

"What everyone seems to be ignoring," says James W. Paulsen of Investors Management Group Ltd. in Des Moines, "is how much the expansion of the 1990s has been driven by investment and supply-side spending."

Since 1989, Paulsen calculates that business capital spending, particularly on computers, has accounted for more than 35% of the rise in real gross domestic product. That's almost three times the postwar cyclical average. As a result, nonresidential fixed investment comprises a record 14% of national output—40% more than in prior decades.

HOW INVESTMENT HAS DRIVEN AMERICA'S ECONOMY



DATA: INVESTORS MANAGEMENT GROUP

Further, even household outlays have been disproportionately driven by "investment" rather than consumption spending. So far in the 1990s, estimates Paulsen, nearly a third of household expenditures have been for investment items such as housing and durable goods (which provide years of service and thus borrow from future consumption). By contrast, the average investment share of household spending in the 1970s and 1980s was only 21% (chart).

All of this suggests that the lopsided supply-side-led expansion of the 1990s is headed for rough going. Demand already seems to be slowing for housing, cars, and appliances. And business capital spending, which has sparked the fastest capacity growth in decades, is likely to slow sharply as the factory operating rate—down three percentage points in the past year—keeps falling.

In sum, says Paulsen, "the economy's fundamental need at this stage of the expansion is for consumption demand to catch up to supply." Yet the omens point in the opposite direction. Government spending is contracting. Job insecurity and scant wage growth have made households tightfisted. Baby boomers, now entering their 50s, are worrying about retirement. And government policy and tax reform seem aimed at enhancing saving even more.

"Everyone favors more investment," says Paulsen. "But my fear is that we may soon be asking ourselves whether saving and investment can sometimes be too much of a good thing."

LAISSEZ-FAIRE'S GLOBAL RATINGS

Free economies lift incomes

What's the world's freest economy? No, it's not the U.S. According to a new index, Hong Kong leads in protection of private property, freedom of exchange, and individual control over business and economic decisions.

The index, published by Washington's libertarian Cato Institute and 10 overseas think tanks, measures freedom on a scale from 1 to 10 in 102 countries. Its criteria range from economic variables such as inflation stability, top marginal tax rates, and government spending's share of national output, to such social indicators as legal fairness and the freedom to open a foreign bank account.

Not surprisingly, economic freedom correlates with income: The 14 top countries, with scores of 9.1 to 6.7, had average per-capita GDP of $14,280 in 1994, vs. $1,650 for the 27 lowest with scores under 4.2. Most of the bottom-ranked nations suffered falling per-capita incomes from 1980 through 1994. By contrast, developing countries with rising economic freedom, such as Malaysia, Iceland, Jamaica, and Chile, saw strong income gains.

THE 10 FREEST ECONOMIES IN 1995

ECONOMIC FREEDOM SCALE FROM 1 TO 10

DATA: CATO INSTITUTE

Not everyone agrees with these rankings, of course. Some might question the high ratings of countries such as Singapore where some sorts of "freedom" seem constrained. And many wonder about Hong Kong once it reverts to Chinese control in 1997. As for the U.S., its rating should rise, the report says, if Washington follows up on plans to cut taxes and government spending.

By Mike McNamee in Washington

GLOOM JUST SHORT OF DOOM

No recession, but zero growth?

If economist Joseph G. Carson of Dean Witter Reynolds Inc. is right, fears of a U.S. recession may climb in coming months. While minimizing the risk of a full-blown downturn, he thinks fourth-quarter growth will be reported as close to zero or even negative.

Signs pointing to a stagnant quarter, says Carson, include disappointing earnings reports from a wide group of industries, a recent slowdown in personal-income-tax collections, and dismal Christmas retail sales. He also figures the strike at Boeing Co. and the federal government shutdowns subtracted at least a percentage point from growth.

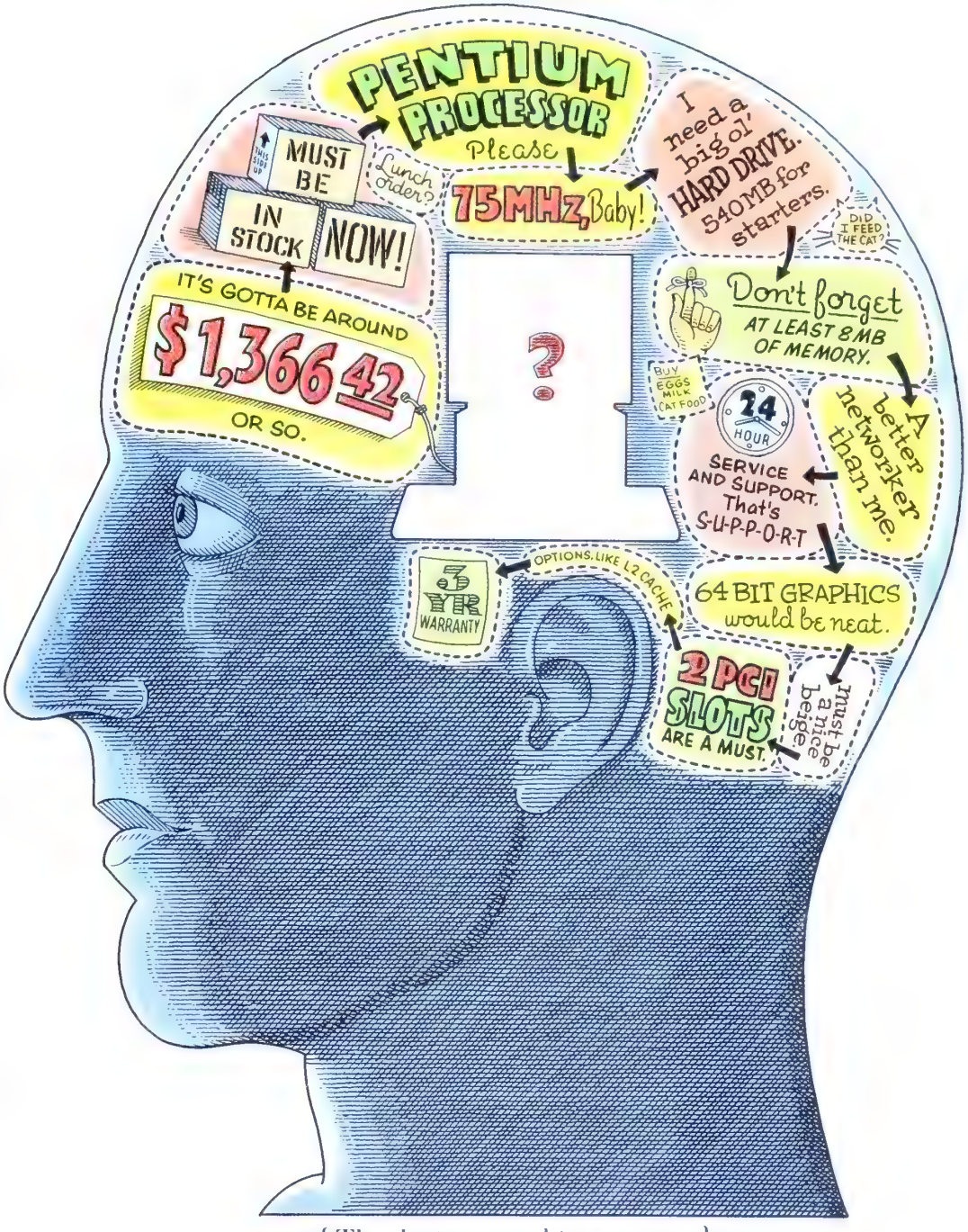
DON'T CHEER YET, STATE TAXPAYERS

A downturn could spark tax hikes

The prevailing political wisdom is that a supply-side philosophy favoring limited spending and low tax rates has taken hold in state legislatures across the U.S. But economist Steven D. Gold of the Center for the Study of the States in Albany, N.Y., is skeptical.

Gold concedes that 30 states cut taxes in 1995 and only seven raised them. But he notes that states usually raise taxes during fiscal crises caused by recessions and then cut them as cyclical expansions replenish their reserve funds. Significantly, the 1995 tax cuts were modest—amounting to only 1% of total tax revenues, while the 1991 hikes equaled 4.8% of annual revenues.

The real test of whether states' tax policy has changed, says Gold, will be their ability to avoid tax increases when the next recession depresses revenues and boosts social spending.



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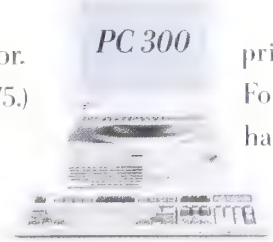

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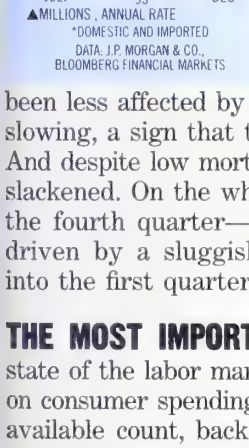
BY JAMES C. COOPER & KATHLEEN MADIGAN

VISIBLE THROUGH THE MURK: SLOWER GROWTH

U.S. ECONOMY It has been a tough winter for economists and anyone else who needs the best possible data to make decisions on investments, business, and—especially—policy. The 21-day government shutdown has prevented the release of any official data since Dec. 18 and has lasted long enough to threaten the reliability of future reports.

Then, just as the government's number factories were ready to get back in business, along came the Blizzard of '96. On Jan. 6, President Clinton signed a continuing resolution running through Jan. 26 that partially funds the data-gathering process. But the severe weather, which has extended the shutdown, further delays data-collection efforts and promises to distort the January numbers even more.

This dearth of good data comes at an especially critical juncture. The available information clearly shows that the economy is slowing. But by how much? The answer is crucial to the Federal Reserve's policy committee, which must sit down on Jan. 30-31—without a reliable picture of the economy—to decide whether interest rates should come down another notch.



What we do know is that consumer spending, though far from robust, is faring better than the dour reports from retailers would suggest. One reason: December car sales were strong, but as with many other retailers, auto showrooms had to cut prices to make deals (chart).

We also know from Federal Reserve data, which have been less affected by the shutdown, that loan growth is slowing, a sign that the overall economy is cooling off. And despite low mortgage rates, new-home demand has slackened. On the whole, the economy's pace slowed in the fourth quarter—perhaps sharply. That slowdown, driven by a sluggish industrial sector, will continue into the first quarter.

THE MOST IMPORTANT thing we don't know is the state of the labor markets—so central to any judgments on consumer spending and industrial output. At the last available count, back in early December, initial jobless claims, a key leading indicator that economists rely on heavily, were rising. December payroll data, originally due on Jan. 6, have been postponed indefinitely.

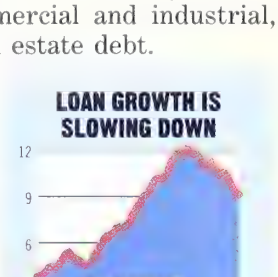
With the government back in business, the delayed data for November and December will be released mostly by the end of January. But by then, they will be ancient history.

The new problem is the reliability of many of the January numbers—and not so much because of the blizzard. The government shutdown has made the collection of accurate January data nearly impossible. Many senior staffers at the Labor Dept. and Commerce Dept. are concerned that relying on surveys of conditions that existed weeks earlier will compromise the integrity of the resulting information.

All this is more than just an annoyance for economists. Policymakers are griping, too. Fed Vice-Chairman Alan S. Blinder says the data drought is starting to become a "serious hardship," and monetary policy will become more of a problem the longer it lasts. Other Fed officials have concurred but say they will just have to make do.

POLICY DECISIONS are crucial right now because the economy's risks appear to be increasingly on the downside. Most notably, loans at commercial banks, while still growing at a healthy clip, are nevertheless slowing down. After peaking at an annual pace of 12.2% in mid-1995, loan growth had declined to 9.3% by the end of December (chart). All categories of loans, from personal to commercial and industrial, have slackened, especially real estate debt.

Somewhat anomalously, personal loans showed strong gains in the final two weeks of the year, despite the disastrous reports from retailers. That could mean consumers were taking advantage of retailers' cutthroat discounts, which indicates the inflation-adjusted sales data will look considerably firmer than the retailers' dollar totals.



The surge could also mean, however, that households are more strapped financially and are thus paying off loans more slowly. Late payments on bank credit-card accounts rose to 3.3% in the third quarter of 1995, the second-highest rate in 10 years, according to the American Bankers Assn.

The explanation probably has more to do with the discounts than with poor finances. After all, consumers were not shy about buying cars in December: Sales of both domestic and imported cars and light trucks hit an

ERIC HOFFMANN/BW

annual rate of 16 million for the month, the year's best showing. Truck sales posted an especially large gain. That showing lifted sales for last quarter above the third-quarter pace, suggesting that car sales were a plus for consumer spending.

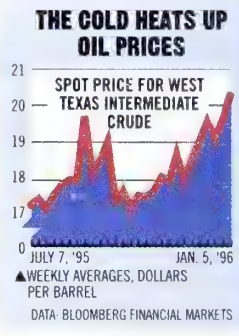
Last month's sales pace won't last, though. Dealers had to offer big incentives to lure buyers. The giveaways averaged $3,000 per vehicle, according to CNW Marketing Research. Still, the strong response is a sign that consumers are willing and able to act on a good buy. While shoppers may be buying fewer coats and scarves, they are certainly plunking down plenty of cash for cars and computers.

HOME BUYING is also holding up well, although fourth-quarter activity appears to have slowed somewhat. For now, data on new-home sales go only through October. But the December builders' survey, taken by the National Association of Home Builders, is highly correlated with the government's numbers and shows a cooler level of activity at yearend.

The survey suggests that the quarter's new-home sales will average well below their third-quarter level of 724,000. And because of the weather, January sales figures are likely to be a disaster.

Another upshot of the bitter weather since December has been the runup in energy prices. High demand on utilities has increased both natural-gas and oil consumption, opening the way for a 13.6% rise in crude-oil prices since the end of November.

The spot price for West Texas Intermediate oil, for example, jumped from $17.83 per barrel in the week of Nov. 24 to more than $20 in early January (chart). Prices are at an eight-month high, which is one reason for the recent advance in overall commodity prices.



Moreover, the price impact could carry over into the spring. Refineries are concentrating on producing heating oil at the expense of their gasoline output. With gasoline inventories already low, drivers could be paying higher prices at the pump when the weather warms. For now, though, the increase is unlikely to raise fears about inflation, especially in the key core rate, which excludes food and energy prices.

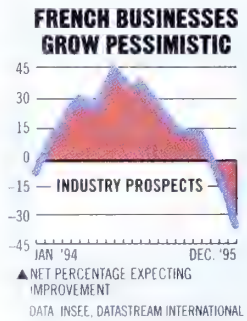
From all available signs, the economy appears in no danger of recession, and the outlook for low inflation and interest rates remains intact. That outlook should be enhanced by an eventual budget deal. But until the government gets its data back on track, everyone from business planners to Fed governors will have to make the best of flying through the fog.

FRANCE

AN ECONOMY STRICKEN BY STRIKE

As France picks up the pieces after a 24-day strike by public-sector workers, it's tallying the damage wrought on the economy.

The latest data from INSEE, France's statistical office, show that business confidence fell in December (chart), and output and orders likely dropped as well. Consumer confidence also slipped, and spending was probably hurt as the rail strike crippled the distribution system. As a result, INSEE calculates that the strike cut at least half a percentage point from growth in the fourth-quarter gross domestic product.



The problem is that France's economy was weakening even before the work stoppage. October's industrial production fell 1.9%, with factory output unchanged. And although consumer spending rebounded 1.4% in November after a 2.1% drop in October, spending so far last quarter is running below the third-quarter average. Private economists forecast that real GDP was flat or slightly down last quarter, after a rise of just 0.8%, at an annual rate, in the third.

The outlook for early 1996 does not carry much hope. INSEE's survey of business expectations suggests that real GDP will grow by 1.5% in the first half. The survey projects further declines in output and increases in unemployment, perhaps lifting the jobless rate from its 11.5% rate in October to 12.1% by the summer.

A weak first half makes it highly unlikely that the economy will reach the growth target of 2.8% set by the government of Prime Minister Alain Juppé. That means the government will not be able to reduce its deficit to 4% of GDP this year. The deficit must slip to 3% of GDP by 1997 if France is to join the European Monetary Union set for 1999.

These recent data, however, make interest-rate cuts by the Bank of France a near-certainty. In deference to the death of former President François Mitterrand, the central bank has delayed unveiling its 1996 policy targets until Jan. 18. But another possible strike at the end of the month will undermine any effort to lift the economy. So, the BOF had better pray for labor peace.

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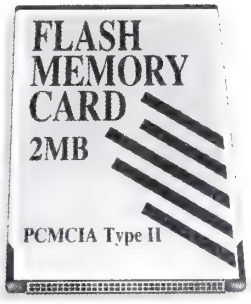

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AUTOS

USED-CAR FEVER

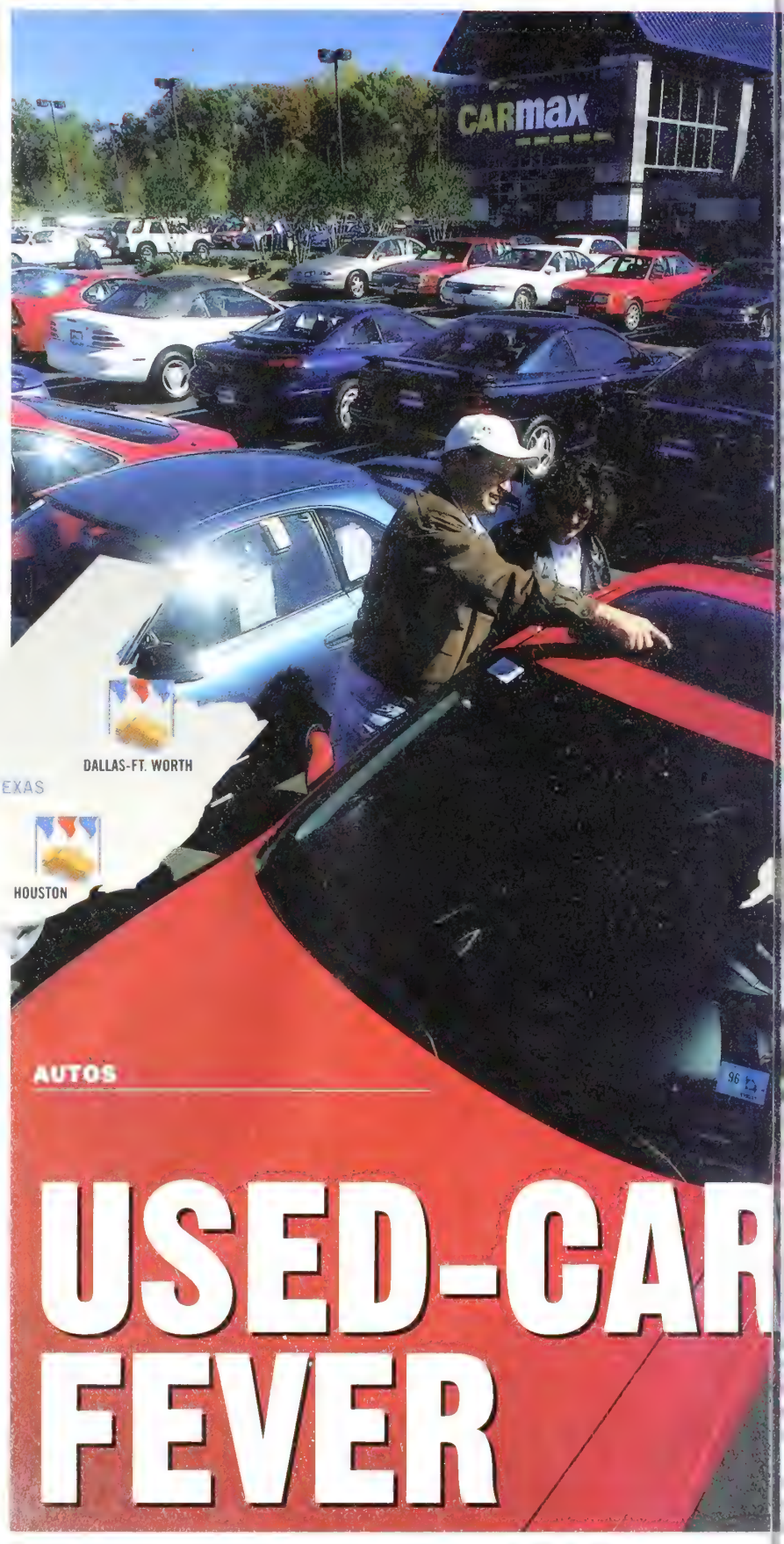
Superstores are spreading. That has traditional car dealers and Detroit quaking

Cynthia Chance bought a used car last year, and (surprise of surprises) she's happy about the whole experience. The 29-year-old Georgetown University graduate student and her husband snapped up a 1992 Honda Accord at a CarMax used-car superstore in Richmond, Va. She doesn't even mind that they probably paid $500 more than if she had comparison-shopped and haggled elsewhere. She prefers the array of choices and pressure-free approach of the auto industry's first category-killer. The process only took two hours and, she marvels, "the whole time we were treated like human beings who were able to decide what we liked."

Consumers such as Chance are scaring the daylights out of traditional car dealers, to say nothing of GM, Ford, Chrysler, and big foreign carmakers. CarMax, a division of Circuit City Stores Inc., on Jan. 5 announced plans to go national, adding seven locations by early 1997 to its current four superstores in the Southeast. Circuit City analysts predict the chain will open 50 dealerships by 2000.

BIG STAKES. Other nascent used-car chains aren't far behind. A group of executives, led by H. Wayne Huizenga, Blockbuster Entertainment Corp.'s former chairman, and Toyota distributor Jim Moran, are launching AutoNation USA, another used-car chain promising to treat customers like royalty. They plan to start by opening three outlets in south Florida this year. More competition is widely expected, with huge retailers such as Wal-Mart Stores Inc. often mentioned as potential players.

At stake is the $275 billion retail market for used cars. So far, the upstarts' toehold is small: Analysts estimate that



SECONDHAND ROWS: *Inventories at CarMax lots range up to 1,000 cars*

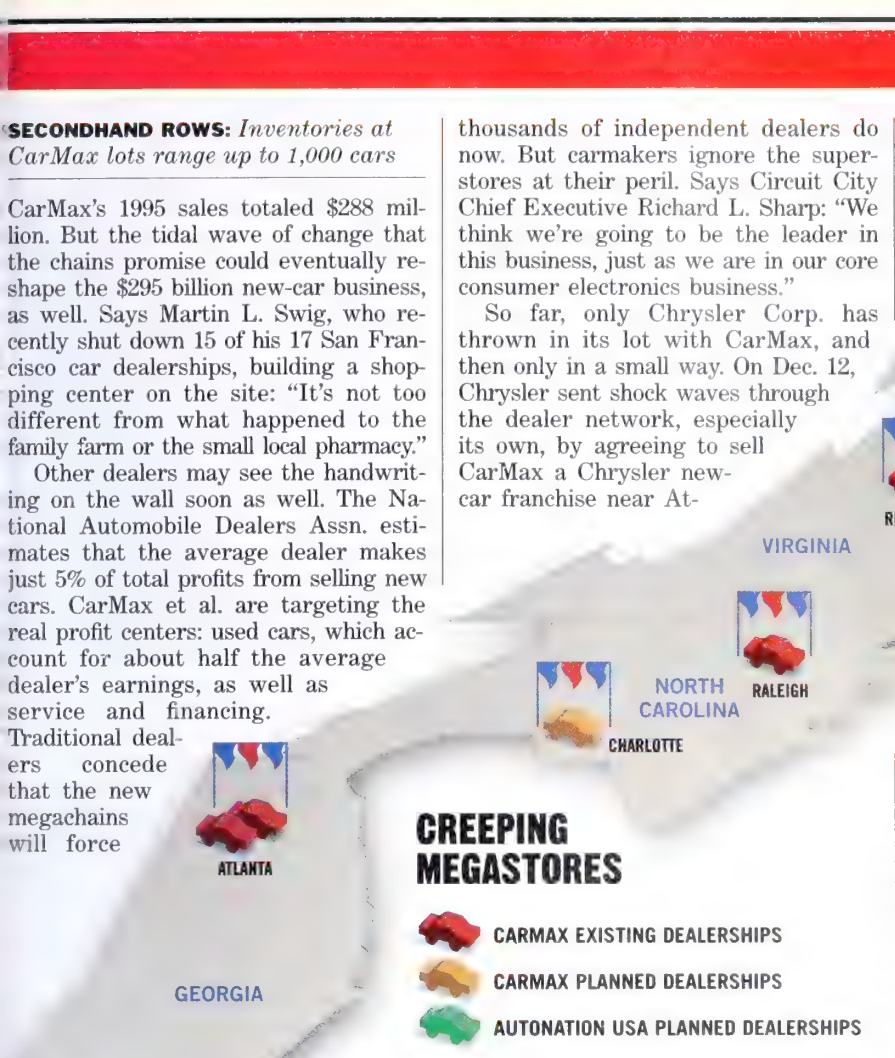
CarMax's 1995 sales totaled $288 million. But the tidal wave of change that the chains promise could eventually reshape the $295 billion new-car business, as well. Says Martin L. Swig, who recently shut down 15 of his 17 San Francisco car dealerships, building a shopping center on the site: "It's not too different from what happened to the family farm or the small local pharmacy."

Other dealers may see the handwriting on the wall soon as well. The National Automobile Dealers Assn. estimates that the average dealer makes just 5% of total profits from selling new cars. CarMax et al. are targeting the real profit centers: used cars, which account for about half the average dealer's earnings, as well as service and financing. Traditional dealers concede that the new megachains will force them to dramatically improve their service. If the new chains succeed, they will squeeze large numbers of new- and used-car dealers alike out of business.

This seismic shift puts giant auto manufacturers in a quandary: Doing business with the used-car chains will undercut, and infuriate, the dealer networks they depend on to distribute new cars. The companies can ill-afford such turmoil, especially at a time when car sales are stagnating and margins are stressed. The growing pressures on Detroit were underscored on Jan. 9 when Ford put $600 rebates and low-cost financing on most of its models.

The car companies also have to be concerned that a few huge retailers will come to dominate distribution, wielding far more clout with manufacturers than thousands of independent dealers do now. But carmakers ignore the superstores at their peril. Says Circuit City Chief Executive Richard L. Sharp: "We think we're going to be the leader in this business, just as we are in our core consumer electronics business."

So far, only Chrysler Corp. has thrown in its lot with CarMax, and then only in a small way. On Dec. 12, Chrysler sent shock waves through the dealer network, especially its own, by agreeing to sell CarMax a Chrysler new-car franchise near Atlanta. Chrysler simply wants to learn about CarMax's approach, says Chrysler President Robert A. Lutz, "because we are convinced that automotive retailing is going to change radically." He knows Chrysler dealers are steamed, but adds: "They don't see the threat on the horizon the way we do."



MANY CHOICES. Crosstown rival car companies say they don't plan similar deals, at least for now. But, says, Ford Chairman Alexander J. Trotman, "quite probably, there will be changes in the future in the total way we do things. We're keeping our options open." Even if the Big Three don't cut extensive deals with the megachains, their Japanese rivals could.

Some dealers worry that the carmakers may end up working hand-in-hand with the megachains—to traditional dealers' detriment. The Big Three have wanted for years to weed out weak dealerships. Plus, the manufacturers' push into leasing cars has rushed a flood of low-mileage, late-model used cars back on the market. Those models, now auctioned off to traditional dealers, are the very kinds of models the megachains focus on selling. If the chains succeed in creating an efficient national market for used cars, they could provide a way to smoothly channel such cars back into the market.

CarMax's focus is on selling top-of-the-line used cars to consumers who shudder at the thought of buying them from a plaid-sport-coated huckster. Modeled on Circuit City's consumer electronics stores, it boasts friendly, low-key sales help who lead customers to computer kiosks. There, touch-screen computers guide customers through the vast inventory of as many as 1,000 cars and trucks. Consumers can choose a handful and print out photos, prices, features, and locations on the store's lot. While a customer is out test-driving a few models, CarMax's computer runs a credit check and its technicians inspect the customer's old car and prepare a written price offer. The entire process often takes less than an hour.

REVOLUTION? Despite the Chrysler deal, CarMax executives insist that, for now at least, their primary focus remains used cars. One measure of how worried many dealers are by even that encroachment in their business: They've never talked faster than they do now in explaining why CarMax and other newcomers are no real threat—at least not to their own business. They're quick to point out that they can undercut CarMax's no-dicker prices, which they claim are $200 to $500 higher than theirs. And they note that CarMax's massive inventories will be a liability when used-car prices erode in the next recession.

Sharp counters that CarMax has hired experienced managers who have gone through past auto slumps. He also says CarMax's gross margins beat the industry average of about 4% and denies that it charges premium prices.

What's indisputable is that auto retailing is ripe for a revolution. Countless studies have found that consumers, as Chrysler Chairman Robert J. Eaton puts it, "would rather have a root canal" than go to a showroom to buy a new car. And if more car buyers learn to love the chains' low-key, no-haggle approach as much as Cynthia Chance did, the car companies may have little choice but to go along for the ride.

By Kathleen Kerwin, with Thane Peterson, Keith Naughton, and Bill Vlasic, in Detroit, and Gail DeGeorge in Miami

THE PAUSE THAT REFRESHES: *Talks are on hold for at least a week*

THE BUDGET

THE O.J. TRIAL DIDN'T LAST THIS LONG

Despite progress, budget negotiators just can't cut a deal

President Clinton and congressional Republican leaders keep edging closer to a balanced-budget accord. But like squabbling CEOs battling over details of a megamerger, the two sides just can't seem to bring themselves to cut a deal. The latest hitch came on Jan. 9, when negotiators suspended talks for at least a week. The news jarred financial markets, leaving traders wondering anew whether Clinton and the GOP really intend to forge a compromise or stall until after Election Day.

A deal to balance the budget by 2002 shouldn't be hard to strike, say budget experts. On many key spending issues, the money differences are too small for Clinton or the Republicans to claim they're standing firm on policy principles (chart). The problem lies elsewhere. "It's short-term politics," laments Martha Phillips, executive director of the Concord Coalition, a deficit-reduction advocacy group.

"UNSETTLING." Wall Street traders, who had been bidding up stock and bond prices in anticipation of a breakthrough, are hedging their bets. Yields on 30-year Treasury bonds soared from 5.95% on Jan. 3 to 6.19% on Jan. 10. The stock market, meanwhile, dropped 97 points the day after the two sides suspended their talks. "If there's more disappointment, bond yields will rise further," warns Philip Braverman, chief economist for DKB Securities Corp.

That could quickly weaken the overall economy. "It's an unsettling factor," says G. Richard Wagoner Jr., president of General Motors Corp.'s North American operations, who worries that if the budget stalemate drags on, interest rates will creep up, hurting car sales. If the negotiations fall through, warns Chicago Mercantile Exchange Chairman John F. Sandner, "I'd expect real turmoil."

One thing seems certain: Arguing over the budget will continue at least until Jan. 26, when another temporary spending bill expires and the government is set to shut down for the third time since November. Then, Washington will go back into crisis mode, and talks will again heat up.

For now, though, Clinton and GOP leaders are getting out of town. Clinton plans to visit U. S. troops in Bosnia. Senate Majority Leader Bob Dole (R-Kan.) wants to campaign in Iowa and New Hampshire for the GOP Presidential nomination. And House Speaker Newt Gingrich (R-Ga.) is off on a fund-raising tour. The hiatus also lets both sides lobby party dissidents who are balking at the prospect of any agreement.

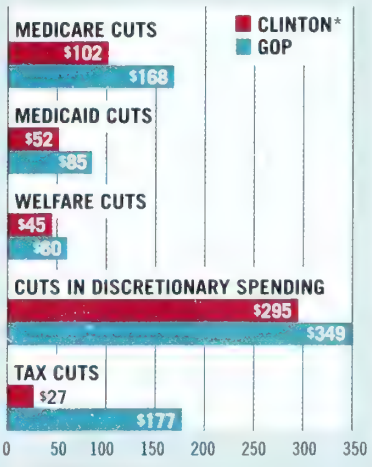
Sources close to the talks say all three principals are itching for a deal and are agonizingly close on many points. For instance, in the high-profile confrontation over Medicare savings, Clinton and the Republicans are separated by $66 billion over seven years for a program estimated to cost nearly $350 billion in 2002.

DOG DAYS. Clinton and Gingrich still have a big job convincing reluctant House members, though. The sticking point: finding a middle ground on tax cuts. There are signs that some GOP lawmakers may soften their tax-cut demands. "Even most freshmen would agree to use savings to balance the budget sooner and come back to tax cuts later," says hard-line Representative Nick Smith (R-Mich.). But others are in no mood to back down.

Clinton's problem

WORLDS APART?

The gap between the seven-year proposals is narrowing, but remains.



DATA: CONGRESSIONAL BUDGET OFFICE

is finding a way to persuade House Democrats to accept a budget agreement that most believe cuts too deeply into Medicare, Medicaid, and other social programs. About 60 Democratic votes are up for grabs on the budget, and White House officials say they will not embrace any agreement without the support of most of that bloc. "It's a delicate balance," says one Administration official. "We're running for the middle, but we can't lose our base."

Increasingly, the key for both sides lies with a group of conservative Democrats known as the "blue dogs." Gingrich vows to cobble together a package with a veto-proof House majority that includes these Dems. Such an alliance seems far-fetched, in part because the blue dogs oppose any tax cuts this year. But as both sides court the Democratic conservatives, they may yet stumble onto an acceptable compromise.

Budget insiders agree on what a final deal will look like—roughly $100 billion in tax cuts, $150 billion in Medicare savings, and $60 billion in Medicaid. Clinton, Gingrich, and Dole are hoping that pressure from the markets and the public will push recalcitrant lawmakers into such a compromise. "They need to close the deal," says Allied Signal CEO Lawrence A. Bossidy. "The people are tired of excuses and fingerpointing." But for now, political one-upmanship appears to be far more seductive.

By Howard Gleckman, with Amy Barrett and Susan B. Garland, in Washington, with bureau reports

COMMENTARY

By Mike McNamee

IMPEACH BOB RUBIN? FOR WHAT? SMARTS?

In mid-February, the Treasury Dept. will again bump up against the $4.9 trillion national debt ceiling. With budget-balancing talks in limbo, Capitol Hill Republicans are eager for a new chance to squeeze President Clinton by denying him the power to borrow money to run the government. GOP leaders vow that they won't raise the limit until Clinton accepts a plan to balance the budget by 2002. They hope that Clinton will cave in to them rather than allow the U.S. to default on $245 billion in interest payments on Treasury securities.

They might as well forget it. The Treasury Dept. has defused the "default bomb," using tools Congress itself provided in Treasury's statutory authority. The only question now is whether the GOP is going to keep playing chicken with the nation's creditworthiness, looking more foolish with every passing day, or drop the threat. For the good of the country—not to mention their own political prospects—Republicans should let Treasury get on with financing past red ink while negotiators concentrate on preventing future deficits.

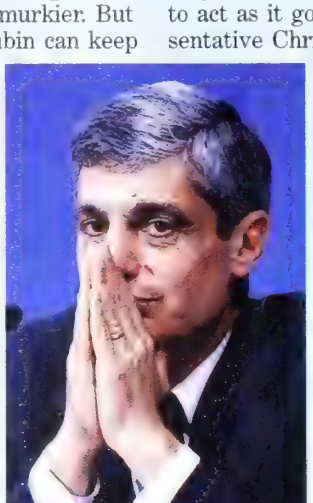
NEW OPTIONS. Treasury Secretary Robert E. Rubin neatly sidestepped the default problem last November. By shifting part of two civil-service retirement funds from one ledger to another, he cleared the way to borrow $61 billion and stave off default. Now, with another debt deadline looming, Treasury lawyers are examining new options—and Rubin's bag of accounting tricks is still more than half full. The likely first moves: tapping some $10 billion in Treasury's foreign-currency accounts and replacing bonds held by some civil-service retirement funds with assets owned by Treasury's Federal Financing Bank to free up over $80 billion for new borrowing.

Each step takes the Treasury chief into a new area where the legal authority for his moves is murkier. But there's no doubt that Rubin can keep up the creative borrowing well past the November elections.

That infuriates Republicans, who felt blindsided when the close-mouthed Rubin made his moves in November. The Wall Streeter's financial maneuverings have done more to weaken the GOP's budget leverage than all the posturing of such political operatives as White House Chief of Staff Leon E. Panetta. Now, many Republicans say that Rubin's gambits infringe on Congress' constitutional power to control the national debt, and some pledge to try to impeach him if he makes it through February's squeeze. "This is not an idle threat," warns Representative David Funderburk (R-N.C.).

Maybe not, but it is stupid as political strategy. Treasury bond prices fell a full 1% just minutes after the impeachment threat was made on Jan. 4. How would the GOP explain to millions of bondholders that Congress was going after Rubin for protecting their investments?

Rubin's high-wire act is risky. His performance last year—first decrying the danger of default, then dodging it with apparent ease—created enormous ill will on Capitol Hill. "Treasury is inventing its legal authority to act as it goes along," fumes Representative Christopher Cox (R-Calif.). In a Jan. 4 letter, Reagan and Bush Treasury chiefs Donald T. Regan, James A. Baker III, and Nicholas F. Brady warned Rubin that bending borrowing rules any further would invite Congress to clip Treasury's wings. But these three also had political motives. They were coaxed into the political fray by House Ways & Means Committee Chairman Bill Archer (R-Tex.) and their own memories of Democrats' debt-ceiling maneuvers. "There's an element of payback here," says a former Treasury aide.



QUICK MOVES Rubin's creative borrowing has defused the GOP's "default bomb," and his bag of accounting tricks is still far from empty

Financial markets had the good sense to discount the default risk in November. That makes it unlikely that Wall Street will deliver the pressure on Clinton that the GOP seeks for a February showdown. If Republicans want to force Clinton to accept their budget priorities, they'll have to do it with hard political bargaining. A debt crisis won't do the trick.

McNamee covers the Treasury Dept.

TECHNOLOGY

POST-WIN95 DEPRESSION SETS IN

Did the tech boom bust–or just high expectations?

Adobe Systems, Symantec, Motorola. One by one, starting on Jan. 5, high-technology companies went public with unnerving news of earnings disappointments. Crash! Jittery investors sent shares of Adobe Systems Inc. down 9%, to 38. Symantec Corp. fell 33%, to 10¾, and Motorola Inc. dropped 19%, to 45¾. Late on Jan. 10, Apple Computer Inc. said it would post a $68 million quarterly operating loss—and its stock sank, too. After 18 months of dizzying performance, computer shares took a bath, driving the tech-heavy NASDAQ down 33 points, or 5.9%.

There was an element of déjà vu in all this. In recent years, technology investors regularly have lost their nerve every three months, just before their companies issue quarterly profits pronouncements. This time, shareholders fretted about lower-than-expected sales of Microsoft Corp.'s Windows 95, about a potential glut of semiconductor capacity, and more than anything, about a slowdown in the booming personal computer business.

EASILY SPOOKED. Analysts responded to the bloodbath as they have to previous high-tech corrections, coolly repeating that the underlying fundamentals fueling the tech boom are still strong. Really, said some market watchers, the problem was one of investors' overheated expectations. "We got too optimistic on the upside, and we're getting too pessimistic right now," says Dan Niles, a chip analyst with Robertson, Stephens & Co. Adding to the sector's volatility: an unprecedented number of nontechnical investors who were easily spooked.

That explanation, though, may be too facile. True, it's premature to declare the tech boom dead. But there are signs that this time, investors may have real reason to grit their teeth. For one, there was Windows 95, the new operating-system software that was supposed to trigger a major buying cycle as customers purchased more powerful PCs and software. Anticipation of such demand powered much of last year's nearly 50% tech-stock runup.

WHOOPS! The pell-mell rush to buy more powerful hardware and compatible software never quite materialized

Microsoft itself is reaping rich rewards from Win95, especially on sales of the software to PC makers who package it with their machines. "Our sales are breaking every record in the book," says Brad Chase, general manager of Microsoft's Personal Systems Group. Although the software giant's stock is down 20% from its high of 103 last summer, it is expected to report fourth-quarter earnings of $540 million, up 46%, on Jan. 18.

But Win95 hasn't exactly delivered the windfall that many other companies and investors were banking on. Take Symantec. The Cupertino (Calif.) software company made a fat bet on Windows 95, rushing to produce one of the first compatible programs on the market. So far, though, its flagship product, a "housekeeping" program called Norton Utilities for Windows 95, has sold far less than the company expected. Citing disappointing sales of its Win95 products, Symantec on Jan. 9 warned investors that its earnings would fall 13% short of estimates.

ON DEAF EARS. Worries about semiconductor overcapacity, though, still appear unfounded. Swept up in the tech-market hysteria last year, chipmakers did, indeed, make investments in expensive new manufacturing facilities. Now that some PC makers are canceling overly optimistic orders, chip prices are falling. But Motorola's 16% decline in fourth-quarter earnings can be blamed partly on a shortage of chip production, not a glut. And most chipmakers and the analysts who watch them believe that the industry will grow by at least the 26% predicted by the Semiconductor Industry Assn. for 1996. In 1995, the industry posted gains of 40%.

In any case, what's bad for the semiconductor industry could be a boon to PC makers: Price drops could boost demand for computers. That's why some analysts say investors are missing the fine points. "To take everyone down because of an abundance of DRAMs [dynamic random-access memories] is a little premature," says John B. Jones Jr., a vice-president at investment bank Salomon Brothers Inc. Terrence Quinn, an analyst with Furman Selz Inc., says concerns about overcapacity and a slow ramp-up for Win95 were raised months ago—but fell on deaf ears. "A lot of these issues were raised last spring, but the market just sailed through it," he says.

Will the optimists be proved right once more? Indeed, tech stocks already were edging up on Jan. 10, and analysts were predicting that the nasty earnings surprises may be over. Then came Apple's latest bombshell. Price-cutting, weaker demand than expected, and thinner gross margins all conspired to beat down revenues, the company said. A new restructuring plan is coming on Jan. 17. And jittery high-tech investors just can't wait.

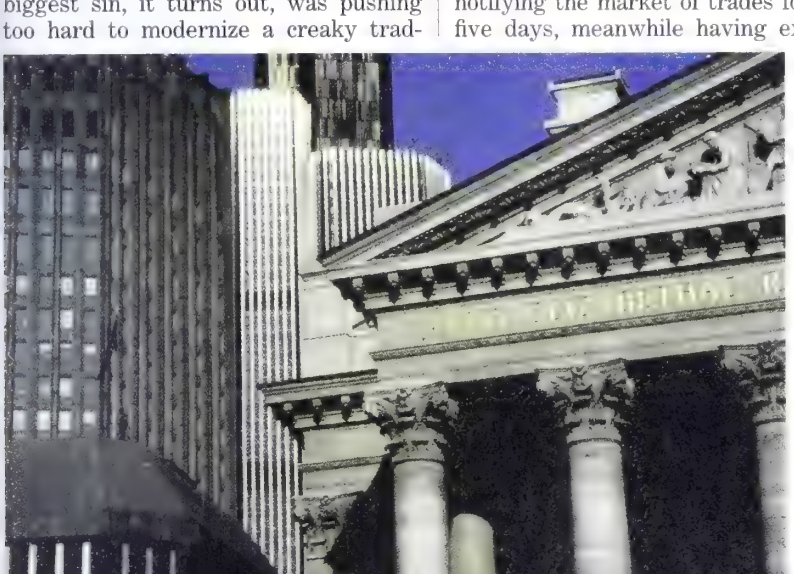
By Amy Cortese, with Jeffrey M. Laderman, in New York, Robert D. Hof in San Francisco, and bureau reports

MODERNIZE THIS OLD-BOY CLUB? RUBBISH!

Resisting reform, the London exchange dumps another CEO

The London Stock Exchange hit new all-time highs in the first week of the new year, after soaring 20% in 1995, but hardly anyone noticed. Far more interesting were the fireworks coming from the exchange's corner office. On Jan. 4, the exchange unceremoniously dumped Chief Executive Officer Michael Lawrence. A terse announcement said he had "lost the confidence of the board." He was given 30 minutes to vacate his office.

Lawrence isn't talking. But his biggest sin, it turns out, was pushing too hard to modernize a creaky trading system. Lawrence upset one of the world's most exclusive old-boy clubs: the 46 companies, called market-makers, that dominate the London exchange. On Jan. 10, the exchange issued a statement reaffirming its commitment to a new trading system. But it pulled back from Lawrence's plan to launch the reforms next August.



THE CITY'S NEW FACE: *High-tech competitors are encroaching*

MULTIPLE PROBLEMS. The upshot: The powerful market-makers have rid themselves of an irritant, but the exchange hasn't solved its problems. London's position as one of the world's top exchanges is in jeopardy. Its trading system is archaic, and other exchanges and new online trading services are encroaching. "London needs to be more efficient and more transparent" with price information, says Laurence Faulkner, managing director of Fidelity Capital Markets (Europe).

The heart of the dilemma is that London relies on the likes of BZW Ltd. and NatWest Markets—the investment-banking arms of Barclays Bank PLC and National Westminster Bank PLC, respectively—to post buy and sell quotes on an electronic bulletin board. These market-makers, which include a number of foreigners, keep trading liquid by risking their own capital on large blocks of shares. But they can also delay notifying the market of trades for up to five days, meanwhile having exclusive access to other market-makers' prices.

Lawrence had hoped to quickly introduce a system in which price quotes would be posted and traded electronically, as in New York and Europe. But market-makers worried about being wiped out by a reform that, as exchange members, they would have to pay for.

Its outdated trading system isn't the London exchange's only problem. Competitors around the world are closing in. Amsterdam, Paris, Milan, and Frankfurt, which handle half the trades in continental Europe, have all installed electronic systems, improving information flow and paring transaction costs.

On Jan. 1, a European Union rule change bolstered the Continent's allure. Brokers licensed in one country can now deal directly on other EU exchanges, without having to go through a local broker. Now, even London's biggest market-makers are abandoning London for the Continent whenever possible.

Even within London, competing exchanges are popping up. One, called Tradepoint Investment Exchange, has all the electronic bells and whistles that the larger exchange lacks. Tradepoint's volume has been minuscule. But it could take off, and members wonder why the LSE didn't develop its own system sooner. "Why did we let private enterprise steal a march on us?" huffs Joseph Lafferty, chief of European equities for NatWest Markets.

A transatlantic rival is also looming. New York Stock Exchange Chairman Richard A. Grasso is trying to lure newly privatized companies in Europe to list in New York. London now lists 524 foreign companies, far more than the NYSE's 234. But the exchange hopes to double that figure by 1998.

WHAT AILS THE LONDON EXCHANGE

INSTABILITY On Jan. 4, the exchange fired CEO Michael Lawrence after market-makers opposed his reforms. Lawrence's predecessor had been forced out two years earlier.

COMPETITION Internet services and the New York Stock Exchange are eating away at London's dominance of cross-border trades.

UNIFIED EUROPE A new directive allows brokers to trade from anywhere in the European Union. Now, London brokers do some business on the Continent.

OUTDATED TRADING SYSTEM The exchange is costly and slow, largely because of its system of 46 market-makers, who profit from the spread between buyers and sellers. Market-makers can withhold trading prices for up to five days.

London is fighting back—in a fashion. To compete with New York, the exchange is taking the low road, pointing out that its regulatory regime is a lot looser than that of the Securities & Exchange Commission. "It's cheaper to list in London because we don't require a lot of unnecessary information. We think institutional investors know what they're doing," says Giles Vardey, the LSE's director of markets development.

The LSE has also invested $150 million in its promised new electronic system, called Sequence, which has an order-matching capability built into it. The exchange has formed a committee, dominated by market-makers, to help decide how and when to launch it. Based on past behavior, it's likely they'll do it their way. Slowly.

By Paula Dwyer in London

OPEN FIELD: *The growing importance of systems acumen may lure new vendors*

As Lockheed Martin Chairman Daniel M. Tellep surveyed the defense-industry landscape last year, he saw the big getting much bigger and the small being swallowed up or fading into irrelevance. His $23 billion giant sat atop the industry heap, but the break-neck pace of mergers still beckoned. "As strong as Lockheed Martin is, this is not a static situation," he says.

Now, the landscape is reshaped indeed. On Jan. 8, Tellep unveiled a $10 billion deal to buy Loral Corp.'s defense-electronics and systems-integration businesses and to take a 20% interest in a new Loral space-telecommunications company. The announcement came just five days after Northrop Grumman Corp. announced it would pay $3 billion for Westinghouse Electric Corp.'s defense-electronics business.

CRITICAL MASS. Why all the action? As Pentagon budgets tighten, electronics and communications are becoming growth businesses. Analysts think the sector will take a growing chunk of defense-procurement dollars as the military upgrades existing equipment instead of buying new fleets of aircraft and ships (chart). "The wave of the future is command and control and electronic warfare," says Brett B. Lambert, vice-president of defense consultant DFI International.

The fiercely competitive, relatively fragmented electronics business has been consolidating steadily for years. Now, more mergers are all but inevitable as companies try to ensure they have the critical mass to survive. The Pentagon has actively encouraged such deals in an effort to reduce overcapacity and so lower its own costs, adopting what wags dub a Noah's Ark approach to industrial policy: Two makers of everything the Defense Dept. needs.

Some industry observers, though, wonder whether the Pentagon might end up with just two animals—a pair of 800-pound gorillas. The U.S. industry is "heading toward two huge megaconglomerates" in Lockheed Martin and Northrop Grumman, predicts Charles A. Gabriel Jr., a Prudential Securities Inc. analyst. Indeed, analysts believe the two most recent acquisitions may finally be raising concerns in the military and with federal trustbusters. The Defense Dept. hoped "the dealmaking would go up and down the food chain," says Jon Kutler, president of investment banker Quarterdeck Investments in Los Angeles. "But the medium- and smaller-size companies are sitting on their thumbs while the big players are getting bigger."

CHINESE WALL? Lockheed Martin and Loral crafted their deal so it wouldn't run afoul of antitrust regulators (though the Securities & Exchange Commission is probing trading in Loral options before the announcement). The biggest overlap in the companies' businesses is in satellites and space, so the transaction calls for creation of a new company, Loral Space & Communications Corp., to house Loral's operations. Loral Chairman Bernard L. Schwartz, who will become vice-chairman of Lockheed Martin, will be chairman and chief executive of the new company. And Lockheed Martin's minority stake likely will create a more palatable relationship for regulators than outright control.

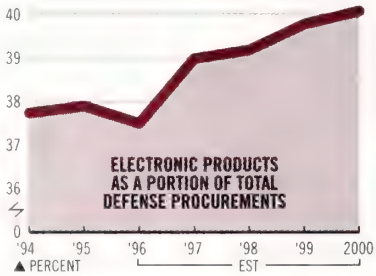
It's a shrewd strategy. In fact, investors generally cheered the deal, sending Loral stock up 23%, to 44½, and Lockheed Martin up 4%, to 80¼. The gains reflected Wall Street's belief that Lockheed will gain from Loral's electronics expertise. The combination probably will achieve some cost savings from layoffs. And its new acquisition will further insulate it from overreliance on any single defense project that could get scrapped as Pentagon cuts continue. The irony: Playing in so many fields at once puts it at greater risk of losing revenue in a broad spending crunch.

Lockheed Martin CEO Norman R. Augustine says that since procurement has plummeted 72% from its high, there's only 28% more to go. "The worst has to be over," he says.

That's probably true for the budgetmeisters' handiwork. Even so, Lockheed Martin may face an even more daunting challenge: Huge commercial vendors that have shied away from military contracting in the past may jump in if procurement reform makes dealing with the Pentagon more attractive. "God help Lockheed Martin the day Microsoft sets up a federal-systems division," says Merrill Lynch & Co. defense analyst Byron K. Callan. That's why it's likely the Loral deal won't be Lockheed Martin's last.

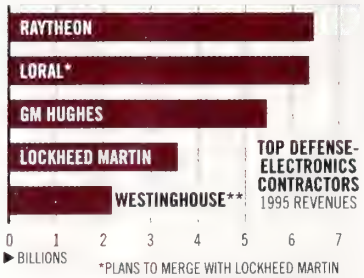
By Stan Crock, with Eric Schine in Los Angeles and Amy Borrus in Washington

MILITARY ELECTRONICS: A BIGGER PIE...



DATA: ELECTRONIC INDUSTRIES ASSN., COMPANY REPORTS

...FOR A SHRINKING FIELD



*PLANS TO MERGE WITH LOCKHEED MARTIN
**PLANS TO MERGE WITH NORTHROP

OUT ONE DOOR AND IN ANOTHER

The news seems unrelentingly grim. Last year, U. S. corporations announced plans to eliminate 440,000 jobs. That brings the number of jobs cut since the start of the decade to 2.9 million, according to Chicago outplacement firm Challenger Gray & Christmas Inc. And 1996 hasn't gotten off to any more promising a start: On Jan. 2, AT&T said it will cut 40,000 jobs. Six days later, Lockheed Martin Corp. and Loral Corp. announced a merger that defense analysts predict could result in several thousand layoffs.

Thanks to greater mobility, corporate job-cutting isn't as lethal as it looks

Look behind the numbers, though, and overall employment in the U. S. is growing. In November, according to the Bureau of Labor Statistics (BLS), there were 1.7 million more people working than there were a year earlier. And the 1.1% net job reductions made by America's largest corporations last year were their lowest in this decade (chart).

TWO TIERS. So where are all those laid-off workers working? And how much are they earning? The answer is vastly different for white- vs. blue-collar workers. Factory workers displaced by foreign competition or new technology generally wind up in lower-paying jobs. Managers, though, face a less desolate landscape. The reason: Corporate America's downsizing continues to be driven by changing strategies rather than by lower profits.

That explains why total employment in the telephone industry, for instance, has risen by 25,000 during the past year, even though the nation's phone companies have eliminated 250,000 positions during the past decade. Nynex Corp. is paring 16,800 jobs, but it also is beefing up sales, marketing, and technical staff to prepare for a deregulated future—often recruiting from other industries.

Marketing, sales, and technical skills, it seems, are always in demand. Take John E. Cummings, a senior analyst of computer-systems development at Continental Grain Co. in Manhattan. The 38-year-old Cummings spent 12 years in a similar position at Turner Construction Co. until he was laid off in May, 1994. He took a six-month break—then landed his new job in just two weeks, at the same salary he was earning before. "I'm rather pleased," says Cummings. "I have more resources here to work with."

Stephen G. Harrison, president of outplacement specialist Lee Hecht Harrison, says about a third of his firm's clients end up with a higher-salaried job, half find work at the same or lower pay, and the rest are self-employed. "I see no indication that high-priced managers are being replaced with lower-priced workers," says Eric R. Greenberg, director of management studies for the American Management Assn. "What we're seeing is that high-priced managers are being replaced with other high-priced managers with different skills."

Certainly, downsizing causes turmoil. Since 1989, nearly 500,000 manufacturing production jobs have disappeared. And past studies show that when blue-collar workers get laid off, their new jobs, on average, pay 20% less than their old jobs did. Even among middle managers, the sense of foreboding is strong. "Managers used to be impervious to changes in the economy," says Paul Osterman, a human-resources professor at Massachusetts Institute of Technology's Sloan School of Management. "Now, they feel like their world is falling apart, even though they are still better off than most folks."

NEW VISTAS. In truth, for managers, at least, restructuring is not one-sided. In its annual survey of 1,000 large and midsize companies, the American Management Assn. found that 50% were planning to cut jobs from July, 1994, through June, 1995. But 60% of those companies were also adding positions. Says Osterman: "We are not turning into a nation of hamburger flippers."

Granted, not all of the new jobs are high-paying, but there can be other rewards. William A. Hensley, 50, was a vice-president at Illinois Bell Telephone Co., a division of Ameritech Corp., when his job was eliminated in 1992. He decided to go to work for a nonprofit, even if it meant less pay. And after looking for 18 months, he took a job as head of public relations for Northwestern Memorial Hospital in Chicago.

At first, he felt crushed by Ameritech's decision, but today, "I'm delighted," says Hensley. "My skills were easily transferable to another industry, and my buyout package allowed me to be discriminating." Let's hope AT&T's laid-off workers feel the same way in 18 months.

By Catherine Arnst in New York

DOWNSIZING THE DOWNSIZING

DATA AMERICAN MANAGEMENT ASSN.

PHOTOGRAPH BY IVAN HERMAN/SEA LIGHT BY A. RUIZ/McNAB

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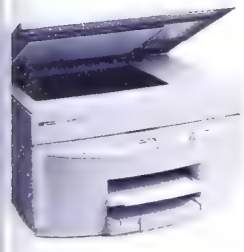

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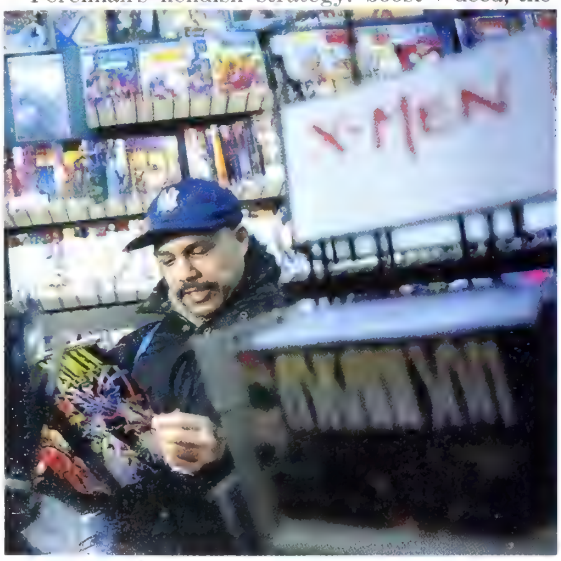
STRATEGIES

WHAT EVIL LURKS IN THE HEART OF RON?

Critics say Perelman is gutting Marvel's comic-book business

Deep amid the glaring yellows, magentas, and cyans, there is a loathsome new villain in Comic Book Land, one as diabolical as Lex Luthor, as evil as Dr. Doom. His name is Ronald O. Perelman. And his weapon, enemies say, is more potent than kryptonite. It's an ax—the one he used on Jan. 4 to lay off 275 of 1,700 employees at Marvel Entertainment Group, the comics-industry leader, of which the billionaire investor owns 80%.

Perelman's fiendish strategy: boost profits by de-emphasizing cartoon publishing and focusing on the low-overhead licensing of popular characters such as Spider-Man and X-Men. He wants to open Marvel theme restaurants in New York, London, and Las Vegas—where he also hopes to run a casino. And he has bought half of a toy company to manufacture Marvel action figures. Perelman's executives have even signed deals to put Spider-Man on candy-bar and fast-food wrappers. From there (evil laugh), the world! Ultimately, the cigar-chomping dealmaker wants to become a major media player, and he is already moving into television production.



BROWSING: *Fans must now buy more issues to keep up*

In fact, Marvel's licensing revenue, mostly from television cartoons and video games, has soared to $50 million from almost nothing in seven years. And CD-ROM and online products are in the works. "The comic book is just one of the ways we can exploit these characters," says Marvel CEO William C. Bevins.

Critics say Perelman is simply bleeding profits from the venerable company—and running it into the ground. "The suits took over. People began to make marketing decisions who knew nothing about the product," says Herb Trimpe, a longtime Marvel artist. Indeed, the company's recent history isn't pretty. A decade ago, Marvel owned 70% of the comic-book market. By 1994, that percentage had plummeted to 32%. Marvel's stock has sunk to 13 from 34¼ near the end of 1993.

EXITING ARTISTS. Marvel has alienated readers by stretching plotlines over as many issues as possible. And stories too often cross over into other characters' books, so fans have to buy more issues to figure out what's going on. "Marvel has no integrity among their books and is in it to make money any way they can," says Jess Nevins, a 29-year-old graduate student and toon fan in Boston. Many top writers and artists, frustrated by such tactics, have left the company.

Marvel admits that, in catering to speculators who stormed the comics market in 1992, it undermined the quality of its books. Now, it says it's weeding out weaker titles, excising such gimmicks as holograms and returning to its old strength: storytelling. While Marvel's plans for a Spider-Man movie are languishing, the company says it will have two major films based on other characters out in time for Christmas, 1996. Such moves may well boost the bottom line. They also may cheer comic-book die-hards still mourning the death of "the old Marvel." Could the evil Ronald Perelman be a hero in disguise? Stay tooned.

By David Leonhardt in New York

REAL ESTATE

WATCH THIS SPACE RACE

Nail that office now. Rates are shooting up in some cities

Looking for better office space? You had better move quickly. The office real estate market, which until last year was as effervescent as yesterday's champagne, is starting to fizz. Gone are free rents and cut-rate renovations for new renters. Instead, vacancies are falling, rents are rising at a double-digit pace, and prime office space is becoming scarce in some markets. Prospects are good enough that savvy investors such as developers Sam Zell, Toronto's Bronfman family, and financier Leon Black are snapping up office properties.

One reason: U.S. commercial office vacancies fell to 14.1% in 1995, their lowest rate in 13 years, according to a new study by office brokers Oncor International. In a few big cities, notably Boston, San Francisco, and Seattle, downtown office vacancy rates are in the single digits (table). What's more, construction analyst F. W. Dodge, a unit of The McGraw-Hill Companies, projects a 12% jump in office-construction starts this year, twice the pace of hotel building—last year's hot sector. Among the projects helped by the upswing: Zell has put Boston's 28 State

OR RENT

. office vacancy
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lion square feet

BEST	
LE	7.1%
N	8.6
RANCISCO	9.9
EAPOLIS	10.1
INGTON	10.6
WORST	
S	35.3%
TON	25.4
IT	25.1
MORE	23.4
NGELES	23.2

ONCOR INTERNATIONAL

Street, a long-vacant 40-story office tower, back on the market

There's no office building boom going on yet. This year's estimated 125 million square feet in construction starts is just a fraction of the 350 million square feet in 1985, when construction starts peaked. But New York-based Turner Construction Co., which is building the 575,000-square-foot Monarch Tower in Atlanta on spec, expects that 15% of its work this year will come from office-building—vs. almost zero two years ago.

The office market is particularly heating up in those regions that are dominated by a few vibrant industries, such as financial services and high tech. For instance, mutual-fund giant Fidelity Investments recently leased 300,000 square feet of new office space in downtown Boston.

LONG-TERM INVESTMENT. Landlords and real estate investment trusts are getting a major boost from the increased demand for office space. Office REITs returned an eye-popping 26.3% last year, tops among Salomon Brothers Inc.'s Commercial Real Estate Composite investment index and more than triple the 7.6% average for all REITs. Salomon analyst John Litt figures that office REITs will return a credible 12% this year, too.

Some big players are betting that office real estate also may be a good long-term investment. The Bronfmans are spending $309 million for a controlling interest in the U. S real estate holdings of Olympia & York Cos., which owns such prime commercial towers as New York's World Financial Center, Boston's Exchange Place, and Chicago's Olympia Center. Financier Black is buying the rest of the O&Y (USA) holdings, which includes office towers in New York and Los Angeles.

The lesson in all this: Any company in the market for digs had better expect to pay more. And don't be surprised if there's a line to look at new space.

By Gary McWilliams in Houston, with Seanna Browder in Seattle and Nicole Harris in Atlanta

RETAILING

PIER 1'S SHIP COMES IN

Even a $20 million trading loss won't spoil a boffo year

It's the kind of timing that makes a CEO want to weep. On Jan. 4, as most retailers posted their worst December sales figures since the 1990-91 recession, Pier 1 Imports Inc., the nation's largest seller of home furnishings and accessories, announced sales gains far higher than those of most retailers. But that rosy performance has gone all but unnoticed. Instead, the chain has been caught up in a wave of adverse publicity over a $20 million loss it announced on Dec. 26, which is widely believed to be the result of inappropriate trading by high-profile money manager S. Jay Goldinger. The financial fiasco, says Pier 1 CEO Clark A. Johnson, "was certainly the Grinch that stole an otherwise fantastic Christmas."

UPSCALE
The retailer's clientele has become more affluent–its income has nearly doubled since 1986

Even with the shortfall, the fiscal year ending Mar. 5 seems certain to be the company's best ever. Analyst Kevin E. Silverman of Everen Securities Inc. estimates annual net income will rise 17%, to a record $35.2 million, even after another $14 million charge, which Pier 1 took last summer to shed its 50% stake in troubled chain Sunbelt Nursery Group Inc. He also expects record sales of $792 million, up 11% from a year ago. Pier 1's same-store sales gain for December was a hefty 16%, vs. an industry average of just 2%, fueling a projected 6.3% rise for the fiscal year (chart).

Pier 1 has bucked retailing trends with a series of well-timed moves catering to nesting baby boomers. Over the past 18 months, for instance, it cut back on apparel sales just as the category tanked. Apparel now accounts for just 6% of sales at the 693-store chain, down from a peak of 14% in 1987. Pier 1 also has accelerated efforts to freshen its product mix. Some 40% of the chain's merchandise, imported from 44 countries, is new at any given time. Nearly 50% of its goods are exclusive to Pier 1. "Our customers know that if they see something they like, they'd better buy it, because if they come back tomorrow it may not be here," says Johnson.

SMARTING INVESTORS. The company also launched its first national TV ads last July. Beginning in April, Johnson plans to shift nearly all of its $40 million ad budget from print to TV. As a result of the strategic changes, the average income of Pier 1's customers has risen from $26,500 in 1986 to $49,100 today.

Many investors, however, worry about glitches that have detracted from Pier 1's strong performance. "Every time they get their ship going in the right direction, they seem to lose credibility," says Mark Boyar, a New York money manager who holds 350,000 Pier 1 shares. Adds Robert B. Buckman, fund manager for Brandywine Asset Management, which holds 1.3 million shares: "Without this situation, I think the stock would be up to 15." Instead, Pier 1 stock hovers around 11, down from its annual high of 12½ in late December.

Investors are angry that it took two years and two write-downs totaling $37.3 million to unwind the disastrous Sunbelt investment. Pier 1 also has yet to explain its recent investment losses. Goldinger's attorney confirms that Goldinger's Beverly Hills-based Capital Insight Brokerage Inc. managed money for Pier 1 but would not otherwise comment. Johnson says Pier 1 will disclose details of the loss in mid-January, after an internal investigation is finished.

A reasonable explanation might be all Pier 1 needs to get its latest financial fiasco behind it. If so, Wall Street could become as enthusiastic about the retailer as stay-at-home boomers already are.

By Stephanie Anderson Forest in Dallas

PHOTOGRAPH BY FREDER JA CHARLES

EDITED BY KEITH H. HAMMONDS

JETT REVS UP TO FIGHT BACK

JOSEPH JETT ISN'T GOING down quietly. The former Kidder Peabody bond trader says he will "vigorously contest" charges from the Securities & Exchange Commission that he schemed to conceal phony bond-trading profits of $348 million. The SEC wants to bar Jett permanently from the securities business and recover more than $11 million in bonuses and salary. In its civil administrative action, filed on Jan. 9, the SEC alleges that Jett ginned up massive profits to mask $83 million in losses. A Jett spokesman says the trader's superiors were well aware of his activity. Indeed, the SEC charged Jett's bosses, Edward Cerullo and Melvin Mullin, with failing to supervise. Cerullo, without admitting or denying wrongdoing, agreed to a one-year suspension from securities work and a $50,000 fine. Mullin will contest the charges.

FIRST UNION'S INSTANT ALBATROSS

GOOD RETAIL DISTRIBUTION wasn't the only thing First Union inherited when it acquired First Fidelity Bancorp. On Jan. 9, First Union agreed to pay $2.29 million to settle charges that FFB's securities arm paid kickbacks to win an underwriting role for a 1990 New Jersey municipal-bond offering. The settlement is the first under the SEC's effort to crack down on "pay to play" kickbacks in the muni business. In late 1994, First Fidelity ousted two officials for their role in the scheme.

DUN & BRADSTREET'S TRIPLE PLAY

DUN & BRADSTREET HAS jumped on the spin-off bandwagon, announcing plans on Jan. 9 to break itself into three public companies. Its A. C. Nielsen consumer-goods market-research service will be spun off, as will Cognizant, a newly named research service for the TV and health-care industries. D&B itself will retain Moody's Investors Service, a debt-rating service, and the Reuben H. Donnelley yellow-page publishing division. The timing was less than stellar: On Jan. 10, as the market tanked, D&B shares gained just 2.3% on the news—though Moody's confirmed its parent's Prime-1 debt rating.

PEERING HARD AT BAUSCH & LOMB

WILLIAM WALTRIP, INTERIM chief executive at Bausch & Lomb, took charge on Jan. 1, and he's already taking action to get the troubled optical company back on track. His first target: the company's inefficient sunglass-manufacturing operation. Waltrip is closing down one plant and paring the workforce at another, cutting a total of 800 jobs. He's also centralizing the sunglass production at three plants, replacing a cumbersome multifactory network. And signaling that the high-living style of former CEO Daniel Gill is history, B&L will sell one of two corporate jets. The company says these and other actions could reduce annual expenses by $25 million.

WHEW! IT MAY BE O.K. TO EAT OATMEAL

OATMEAL: HOT, DELICIOUS—and now FDA-approved. In a precedent-setting proposal, which was made public in early January, the Food & Drug Administration would allow cereal makers to advertise that daily consumption of low-fat foods containing oatmeal and oat bran may reduce the risk of heart disease. Current regulations permit food companies to make only vague health claims for specific products. The proposal is still subject to a 90-day comment period. Not surprisingly, it drew enthusiastic cheers from oat purveyors such as General Mills and Quaker Oats.

ET CETERA . . .

- Boeing won a $4 billion order from Malaysian Airline System for 747 and 777 jets.
- Wellpoint will expand outside California, buying a Massachusetts Mutual unit.
- News Corp. is negotiating for European TV rights to the Olympics from 2000 to 2008.
- AT&T renamed its Global Information Solutions unit, once NCR. The new name: NCR.

CLOSING BELL

COMING UP SHORT

Supercuts' makeover may have come too late. On Jan. 4, the haircutting chain's directors ousted CEO David Lipson. Now, it seems earnings may not cover loan payments. Lenders O.K.'d a one-time advance of $1 million, but shares tanked anyway, dropping 26%. Investors say Supercuts' credibility has been sheared by lawsuits from fired executives accusing Lipson of cooking the books. And Supercuts' entry into New York has led to three disappointing quarters.

HEADLINER: ROBERT GREENHILL

NO LONGER EARNING IT AT SMITH BARNEY

In June, 1993, Robert Greenhill left Morgan Stanley to head Travelers' Smith Barney unit, lured by one of the highest Wall Street pay packages ever: $24 million in salary, bonus, and restricted stock—not including stock options. Now, just 2½ years into his five-year contract, Greenhill is leaving to start an investment-banking boutique.

The departure is an embarrassment for Sanford Weill, Travelers' chief executive. While Weill says that he and Greenhill remain friends, he can't be happy with the millions in compensation that Greenhill will still receive in 1997 and 1998. "It is expensive," Weill admits. In 1994, Greenhill's pay amounted to $6 million.

But Weill had likely gotten a mite tired of Greenhill's lackluster results. Moreover, Greenhill's recruits from Morgan Stanley clashed with lower-paid Smith Barney executives.

For his part, Greenhill notes that Travelers stock almost doubled in 1995 and says: "I think I did have something to do with it."

By Leah Nathans Spiro in New York

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EDITED BY OWEN ULLMANN

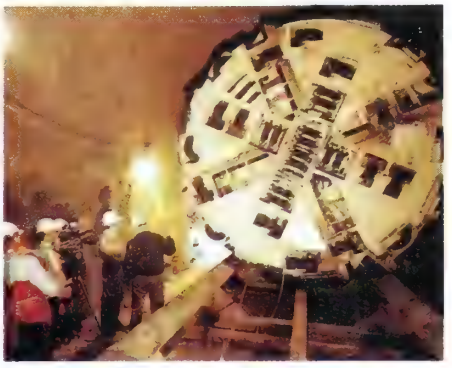
A BRAWL IS BREWING IN THE LABORATORY

For decades, science and technology have been among Washington's most pampered budget babies, usually winning hefty increases year after year. No more. While Republicans and Democrats alike profess continued love for research and development, the grim reality of trying to balance the budget guarantees painful cuts. And that could trigger a nasty squabble, as competing members of the science community grab for their slice of a shrinking pie.

In the GOP budget plan, nonmilitary R&D funds—now $34 billion a year—would drop a staggering inflation-adjusted 32% by 2002, the American Association for the Advancement of Science estimates. President Clinton's plan isn't much better: It calls for constant-dollar cuts of up to 20%, says the AAAS. Although the final reductions aren't expected to be that draconian, they're "going to be ugly," laments a top Senate staffer. Who will fare best? The Republican favorite: basic research. The biggest loser will likely be Democratic-backed applied work in academe and industry.

FRATRICIDE? Predictably, the R&D lobby has raised dire warnings that the nation's future is imperiled. "To cut the R&D budget below present levels is suicide," argues Mary L. Good, Undersecretary for Technology at the Commerce Dept. But scientists are bracing for this new austerity. At the National Institutes of Health, Director Harold Varmus plans to trim costly in-house clinical research and is warning biomedical scientists to tighten their belts.

The adjustment could be far worse. "There's real potential for fratricide," says John Yochelson, president of the Council on Competitiveness. Research leaders hope it won't come to that. "If we fight among ourselves over what crumbs are left, we will destroy ourselves," says David L. Goodstein, physicist and vice-provost at the California Institute of Technology.



IN PERIL: *Collider-style projects*

The clashes have already begun. Last fall, the National Academy of Sciences issued a report on how to allocate funds. Among the university-dominated panel's suggestions: Funding should favor academe. And the report suggested that the national laboratories get too much cash.

To many, those are fighting words. "It's a pretty craven attempt by the university community to claim their piece of the pie," says William G. Morin, technology policy chief at the National Association of Manufacturers. Still, Morin admits that companies might also be tempted to make a grab for national lab dollars to offset potential cuts in federally funded industry R&D.

But neither universities nor industry will get that cash without a battle, lab supporters retort. Labs such as Sandia and Los Alamos in New Mexico have already absorbed budget cuts. More important, the huge facilities have powerful supporters, including the state's two senators—Republican Pete V. Domenici and Democrat Jeff Bingaman—and Steven H. Schiff (R-N. M.), chairman of the House subcommittee on basic research. Going after the lab budgets is "not a winning strategy," warns a key Hill aide.

Unfortunately, the R&D community doesn't yet appear to have a better survival strategy. "The age of denial is over, but I don't see any evidence of people doing anything very constructive about it," says Goodstein. Former House Science Committee staffer John D. Holmfeld says that while a few officials such as the NIH's Varmus are warning of impending cuts, scientists still hope that "they may be able to convince Congress to resume substantial growth for R&D." If that attitude persists, watch out. When the budget crunch really comes in the late '90s, the skirmish to claim a share of the shrinking pie may turn into an all-out food fight.

By John Carey

CAPITAL WRAPUP

STATE OF THE UNION: GREAT!

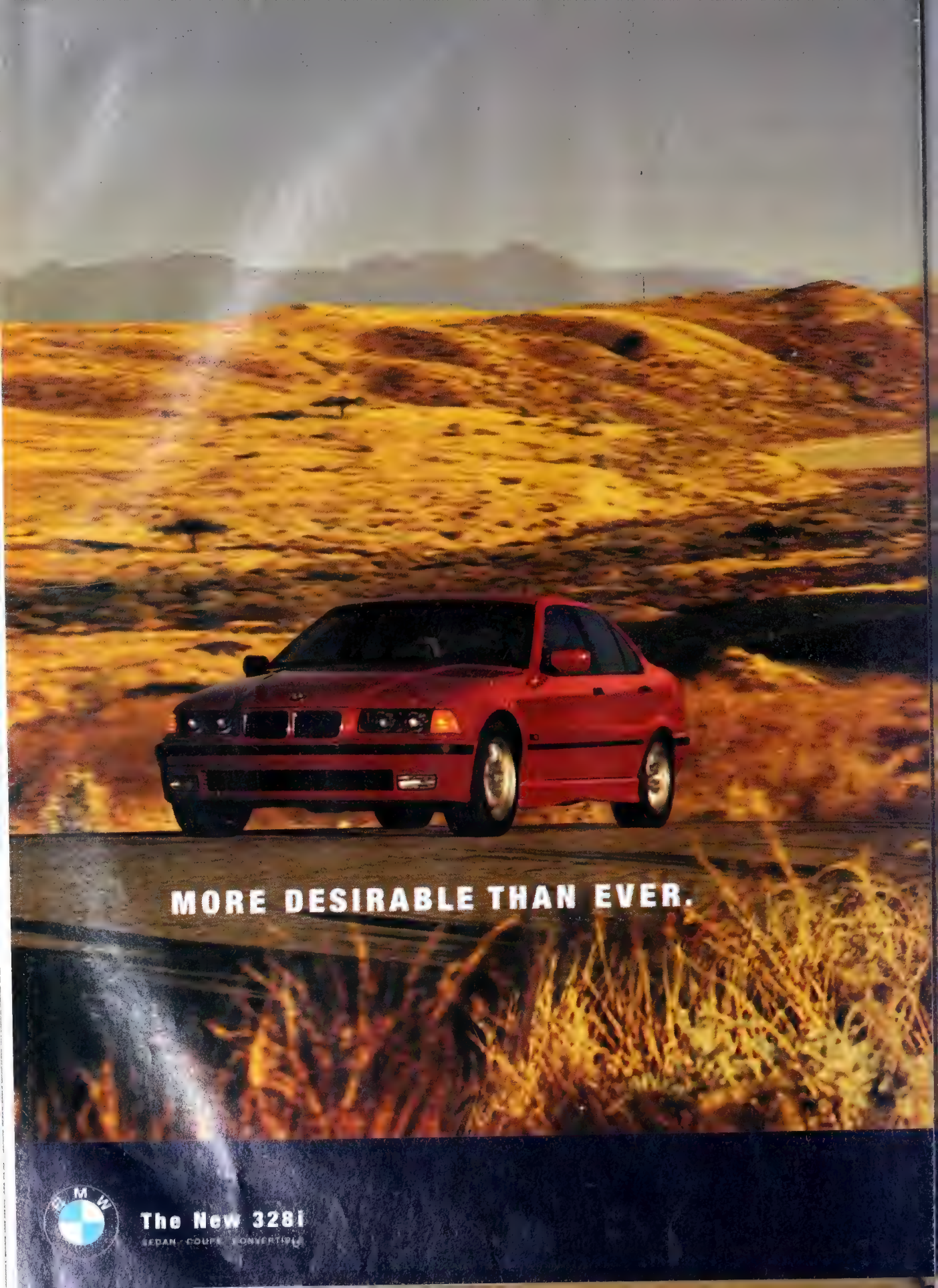
▶ Top White House advisers want President Clinton to use his Jan. 23 State of the Union address to trumpet Washington's positive role. Although "government" is a dirty word to Republicans, Clintonites believe the President should emphasize the problems encountered during the federal shutdown. Clinton is expected to devote the bulk of his speech to a recitation of the nation's strong economic performance on his watch, including creation of 7 million jobs.

ANOTHER WORD FOR NEWT

▶ The Democratic National Committee is lynching House Speaker Newt Gingrich in cyberspace. A new offering on the DNC home page on the World Wide Web—http://www.democrats.org/hot/—is the word game "Hangman with a New(t) Twist." Correctly guess a letter, and a Newt quote pops up. Guess the 9-letter word describing the Speaker (hint: it begins with an "e"), and the computer responds, "You got HIM! Or did he hang himself with his own words?"

KANTOR'S TRUCK STOP

▶ GOP lawmakers are assailing U. S. Trade Representative Mickey Kantor for reneging on a NAFTA pledge just as he's launching a program to enforce trade accords with other nations. Kantor, citing safety concerns, is blocking Mexican applications to operate trucks on border-state roads. Fifteen House GOP free-traders, led by Jim Kolbe of Arizona and Bill Archer of Texas, say Kantor is playing politics: The Teamsters Union wants to keep Mexican truckers out.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JAPAN

AT LAST—SAYONARA TO THE BLAHS

A recharged Japan Inc. is spurring a rebound

Investors think they have plenty to smile about in Japan. Sensing an economic turnaround, foreign money managers have pumped nearly $35 billion into the Tokyo stock market in the past six months, pushing the Nikkei average to 20,600, up 42% from its 1995 low. Market pros think a further gain of 10% to 15% is in the offing this year. Why? After four years mired in the muck, the economy finally is showing signs of pulling out. Most economists expect the gross domestic product to grow more than 2% this year and nearly 3% in 1997.

The reasons for a recovery are clear. The Bank of Japan has slashed interest rates close to zero, and the super yen has retreated from its record highs of last spring. Some $519 billion in fiscal spending packages since 1992 has helped as well, as has a pickup in consumer spending, which accounts for 60% of GDP. And a wave of cost-cutting, restructuring, global investments, and product innovations has Corporate Japan beginning to feel its oats again. Analysts say manufacturers' profits will rise 29% in fiscal 1995, which ends Mar. 31.

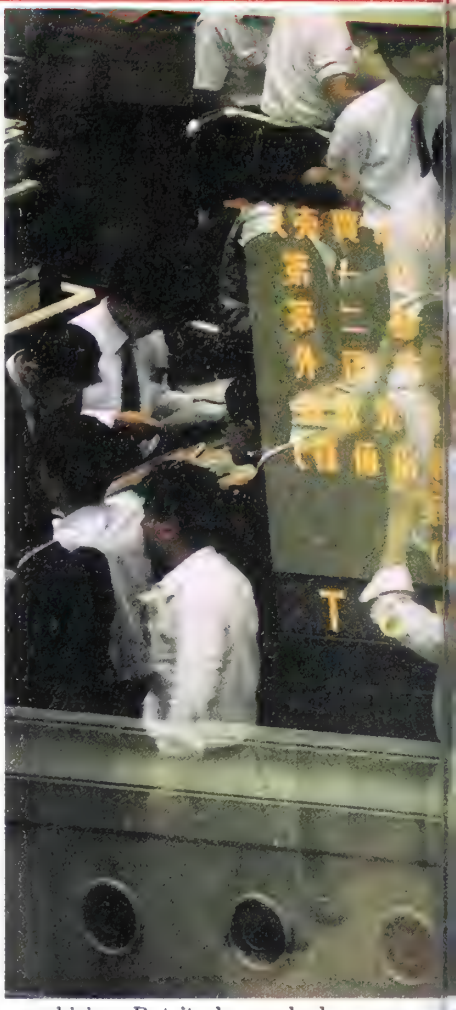
HIGH-PROFIT LINE: *Lexus' LX450, a Range Rover rival, is made in Japan*

SECOND WIND Japan's multinationals are expanding production overseas and cutting overhead at home

With the arrival of Ryutaro Hashimoto as the new Prime Minister, signs of Japan's political paralysis lifting are also cheering investors. True, squabbling politicians haven't pushed through any of the sweeping structural reforms needed to help hard-hit pockets of the domestic economy—especially midsize manufacturers, wholesale distributors, and mom-and-pop retailers. And though the Ministry of Finance has begun to deal with the nation's $350 billion in bad debts, it will be years before the job is complete. But Hashimoto, who has been Minister of both Finance and International Trade, is expected to expedite a cleanup of the banking mess while undertaking some deregulation and smoothing relations with Washington. His political fortunes can only be aided further by signs of a rebound.

And any recovery will owe a great deal to Japanese multinationals, which once again are doing whatever it takes to improve their competitiveness. When the yen spiraled to 80 to the dollar last spring, they moved even faster to cut costs by expanding global manufacturing and parts procurement while taking a hatchet to overhead at home. Now, they are stepping up their capital investments, which are expected to rise as much as 10% in 1996, after a flat '95 and declines in the previous three years. Indeed, manufacturers, more than ever, are capitalizing on a global base for production and setting costs. The result? Not only are their profits up, but "Japanese companies have become more competitive than before," says Seiichiro Yonekura, an associate professor at Hitotsubushi University's Institute of Business Research.

Take Fujitsu Ltd., Japan's biggest computer company. It saw profits slide in 1993 and '94 as its core mainframe computer business stumbled. Shocked, it eliminated nearly 10% of its workforce through attrition and a clampdown on new hiring. But it also pushed up overseas production and started plowing investment into such fast-growth segments as flash memory chips, personal computers, and software. Moreover, it began moving less sophisticated manufacturing abroad. It has started making components for disk drives in Vietnam and will start assembling notebook PCs in Oregon.



BIGGEST BENEFICIARIES. The bottom line: Fujitsu's stock is at a five-year high, and its group net profit should double, to a record $857 million in fiscal '95. And there's room for future profit gains, with executives in no mood to rest on their laurels. Even at 105 yen to the dollar, notes President Tadashi Sekizawa, "salaries are still very high by international standards. We have to reduce the numbers more."

These technology giants clearly are catching a second wind. Toshiba, NEC, and Fujitsu, which have a 39.5% share of the global semiconductor market, were the biggest beneficiaries of last year's 40% jump in sales of dynamic random-access memory chips. And while electronics manufacturers are leaping ahead,

Japan Turns A Corner

DATA: BZW SECURITIES RESEARCH, BLOOMBERG FINANCIAL MARKETS, JAMES CAPEL PACIFIC LTD

HAPPY DAYS: *Market pros see a further gain of 10% to 15% this year*

auto makers also are advancing. To be sure, they are struggling with a capacity overhang of about 4 million units a year at home. But they logged a 4.8% gain in Japanese auto sales in 1995, the first advance since 1990. More important, they are continuing to move production overseas to make high-cost domestic plants less of a burden.

Toyota Motor Corp., for instance, now has a global network of 52 assembly and parts plants to fall back on. Last year, Toyota turned out 350,000 U.S.-made engines, up 50% from 1994. Not only did the move reduce the volume of expensive Japanese engines in U.S.-made cars but it gave Toyota extras to ship back home. At the same time, Toyota is stepping up its assault in the U.S. Like electronics makers that are focusing on manufacturing high-profit lines at home, Toyota will soon roll out a new four-wheel-drive luxury offering, the LX450, through Lexus dealers in the U.S. Targeted at the Range Rover set, the new Lexus will sell for $49,800.

Other players, meanwhile, are doing something once thought unthinkable—breaking ranks with traditional suppliers to cut costs. Nissan Motor Co., for example, recently kissed off longtime supplier Jidosha Kiki Co. and went outside its *keiretsu* family to buy brake components from Aisin Seiki Co., 21.8%-owned by Toyota. To save even more, Nissan aims to cut 7,000 jobs by 1998. All told, such cost-cutting has enabled the industry to lower its breakeven point to 95 yen to the dollar, from 100 a year ago, estimates Morgan Stanley & Co. analyst Koji Endo. That is taking the pressure off auto makers to order major plant closings at home.

CRASH DIET. But Japanese companies still have a lot more restructuring ahead. While much of Japan Inc. has gone on a crash diet, it still remains dramatically overemployed. Most of the job cuts so far have come from fobbing off older workers to affiliates and simply not hiring new graduates. As a result, Japan's record 3.5% jobless rate likely will rise.

Sustaining an economic recovery also will require a broader cleanup of Japan's banking mess. Several big commercial banks that founded and lent to housing-finance companies called *jusen* are being forced to forgive $33 billion in bad credits to the collapsed industry. If the banks start selling equity holdings to cover these losses, the Nikkei's rally could end. Analysts also question whether Prime Minister Hashimoto will be able to further stimulate the economy. Kenneth S. Courtis, chief economist at Deutsche Bank Capital Markets (Asia), estimates Japan's budget deficit should hit 4.2% of GDP in 1996, against 2% in the U.S.

But even if the government can't spend much more, the economy seems poised for an advance. Japan's top-flight multinationals have cut costs to the bone. Business investment is on the mend. Money is easy. And a rebounding Nikkei is lifting overall sentiment. To be sure, a rising Nikkei seemed to herald an economic rebound in 1993 and '94, only to sputter out when the recovery failed to materialize. This time may be different. After a nightmarish ride in the early 1990s, the Japanese economy may finally get a reprieve.

By Brian Bremner and Steven Brull in Tokyo

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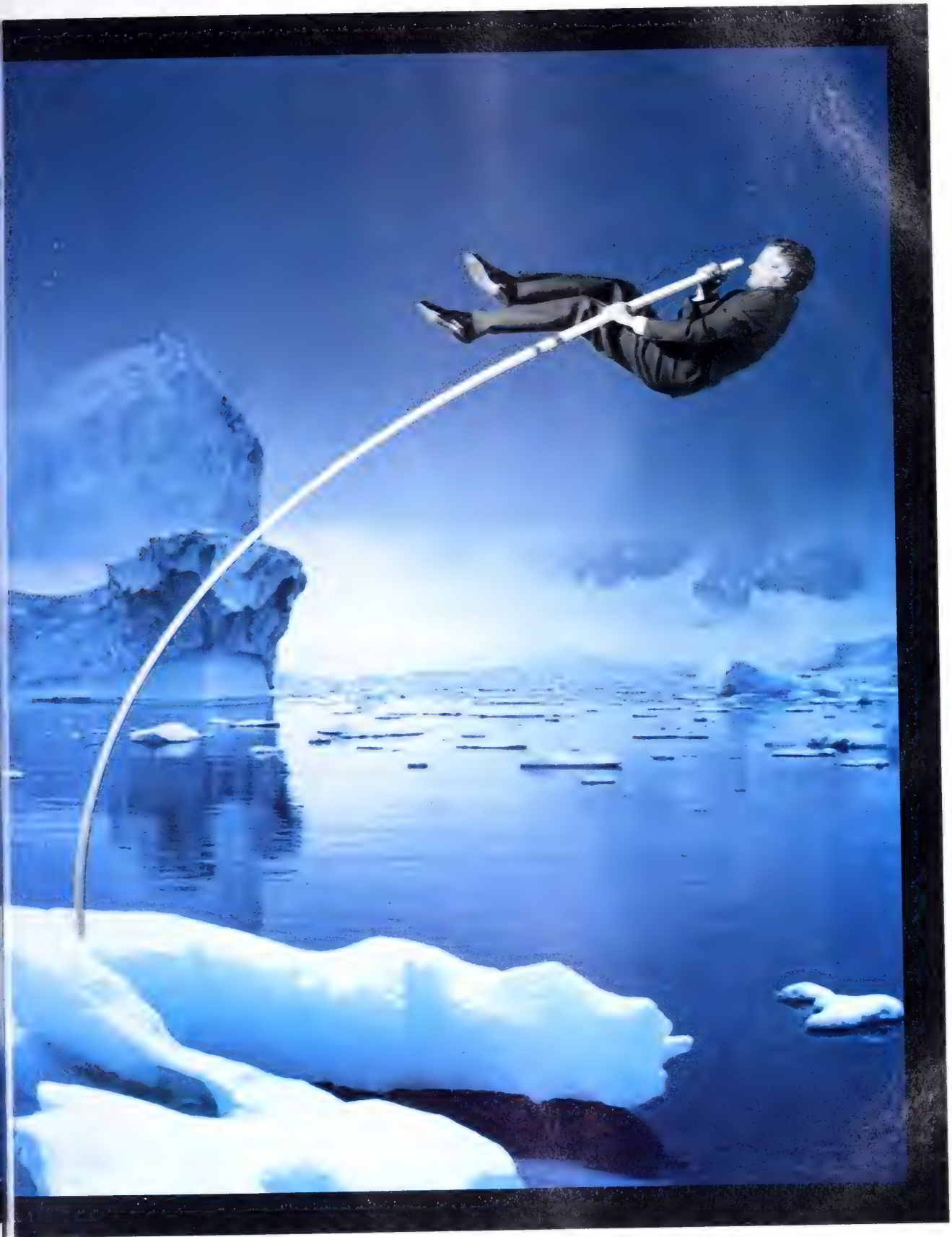


FRANCE

UNDER SUSPICION: *LE TOUT* BUSINESS ELITE

The crackdown on corruption looks likely to widen in '96

For France's business Establishment, the new year is off to a disturbing start. Within recent weeks, three of France's most respected business leaders—the chief executives of Renault, Paribas, and Bouygues—have been placed under investigation by French magistrates for allegations ranging from bribery to accounting fraud. And sources say a fourth manager, the former CEO of oil giant Elf Aquitaine, is likely to face interrogators soon.

The surge of top-level probes is a sign that the magistrates' two-year-old crackdown on high-level business corruption is moving into high gear. Since last spring, investigators have been concentrating on political figures and even sent Alain Carignon, a Cabinet minister, to prison. Investigators "have broken the taboos for politicians," says Thierry Jean-Pierre, a former investigator who won a European Parliament seat last year. "Now we'll see taboos broken in business," he believes. That means the attack on France's cozy business practices is likely to widen in 1996.

"OUTRAGED." Under scrutiny is a veritable who's who of French business (table). Ironically, one investigation focuses on André Lévy-Lang, the U.S.-educated boss of investment giant Compagnie Financière de Paribas, who has promoted corporate governance in France. And sources say Löik Le Floch-Prigent, the former Elf Aquitaine CEO, will soon face interrogators. Investigating judge Eva Joly is "outraged" that he was recently named to run the French state railway, despite her year-long probe of his alleged misdeeds at Elf in the early 1990s. She is speeding up the case and will soon haul him in to justify his actions, the sources say.

Not just judges are chasing corporate wrongdoers. Colette Neuville, France's top shareholder rights advocate, has been exploring last summer's failure of a bank, Banque Pallas-Stern. She says she'll soon ask prosecutors to file fraudulent accounting charges against several elite outside executives who were involved with the bank.

Smaller prey are also being chased. Early in January, 30 chefs were hauled in from such top restaurants as Tour d'Argent. The chefs are suspected of taking kickbacks from food suppliers. Some 350 Paris apartment managers are being grilled for graft on heating and repairs.

To be sure, the new crop of probes could fizzle. In the past two years, investigators have begun working on two dozen big business cases. Only one has produced a noteworthy result so far: Pierre Suard lost his job as chairman of Alcatel Alsthom last April. He awaits trial on charges of fraudulent billing.

Moreover, no formal charges have been brought against the three latest CEOs under investigation. Judges have declared a *mise en examen*—a procedure requiring the executives to explain away suspicions. After listening, the investigators either file charges or drop the case.

IMAGE CRISIS. The inquiries hitting the big targets have been under way at lower levels for months. Renault CEO Louis Schweitzer is under investigation for possible misdeeds in a government job a decade ago. At Paribas, sources say Lévy-Lang requested a *mise en examen* to help clear the bank's name. Neither they nor the other executives recently implicated in probes—Le Floch-Prigent and Martin Bouygues—would comment.

But whatever the circumstances, it's a blow for France's top companies to have CEOs implicated in corruption probes. "It's absolutely terrible for our image," says an executive of one company. Renault officials fret that the planned sale of the government's remaining 51% stake in the company could suffer, even though the Schweitzer probe has nothing to do with Renault.

As the magistrates dig up fresh dirt, the impact of their investigations could be felt across Corporate France. Jean-Marie d'Huy, the judge who investigated Suard and who specializes in business fraud, acknowledges that corruption in France "doesn't touch all companies by any means, nor all of society as it does in Italy." Yet, he argues, French companies are fraud-prone because power tends to be concentrated at the top. If the growing crop of investigations bears fruit, some of France's elite managers may not be exercising that power much longer.

By Stewart Toy in Paris

RENAULT'S SCHWEITZER

PARIBAS' LÉVY-LANG

A New Crop of Corporate Probes

COMPANY/CEO	ISSUE
RENAULT Louis Schweitzer	His role in alleged wiretapping as a prime minister's aide in early 1980s. Also involved in a tainted-blood scandal.
PARIBAS André Lévy-Lang	Alleged false accounts at cement producer Ciments Français, some of whose shares Paribas sold to Italy's Italcementi in 1992.
BOUYGUES Martin Bouygues	Allegations of improper payments to a politician and collusive bids with competitors on construction projects.
ELF AQUITAINE Löik Le Floch-Prigent*	Under investigation for allegedly accepting cash for investing company funds in Bidermann, a French clothing producer.

*Former CEO

DATA: BUSINESS WEEK

COMMENTARY

By Stewart Toy

THE LEGACY OF A POLITICAL CHAMELEON

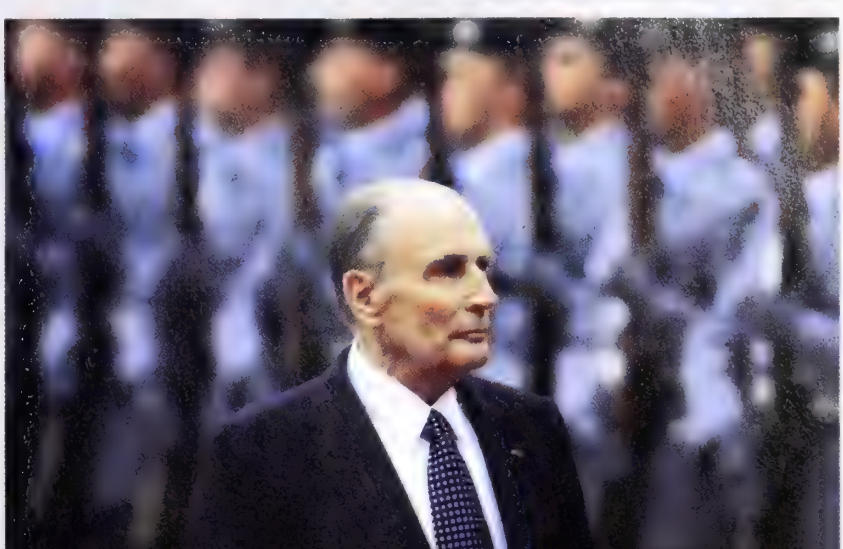
François Mitterrand was a cynical politician who swayed from right to left over his lifetime as opportunity called. Once he staged a phony assassination attempt on himself to win sympathy. Yet this complex French President, who died on Jan. 8, ranks as one of Europe's most significant leaders of this century. He remade France—in a more positive way than many critics realize—even if he didn't always intend to.

Mitterrand put France through a foolish socialist experiment at the start of his 14-year reign, nationalizing industry and lavishing benefits on workers. It was doomed from the outset in a free-market world. But it was an experience that France needed to get out of its system, given its heritage of a militant left that rarely ruled but posed a constant disruptive threat. Mitterrand won socialism the chance to govern. As a result, he unintentionally destroyed it and produced a healthy centrist consensus in the once-polarized country.

As a political chameleon, Mitterrand served France well by switching course only a year after his 1981 election. Although he continued to pay lip service to socialism, Mitterrand saw that France needed a dose of liberalism if its industry was to survive global competition. He spent most of his tenure liberalizing the regimented economy he inherited. He killed controls on wages, prices, and capital. He let companies lay off workers without government permission and ordered state companies to make a profit. Only a Socialist could have gotten away with it.

LONGEVITY'S COSTS. It's true that the late President didn't go far enough. He refused to privatize industry, and he let bureaucrats micromanage the economy. Still, his reforms led to a wave of industrial restructuring that boosted French efficiency. In almost every year of his reign, which ended last May, productivity grew faster in France than in Germany.

Mitterrand also made France a more positive force internationally. Although his vision of French *grandeur* differed little from that of his early archrival, Charles de Gaulle, realist Mitterrand accepted that France could no longer go it alone. He moved closer to NATO and built more cordial ties with the U.S.



COMPLEX VISION: *Socialist Mitterrand made France more competitive*

But European integration became Mitterrand's top priority. Unlike his predecessors, who waffled between cantankerous nationalism and inaction, he realized that a diminished France needed Europe more than the other way around. He became the biggest promoter of a united Europe—even giving up part of France's sovereignty by letting Brussels control product standards, antitrust policy, and other rules. An unstated goal was to harness Germany in a French-run Europe.

Europe, of course, is not turning out as Mitterrand hoped. A reunified Germany is proving less willing to jump through hoops. Part of the blame lies with Mitterrand himself. He never quite comprehended Europe after the fall of the Berlin Wall and seemed paralyzed in dealing with Europe's new order. As he aged, Mitterrand reverted to old French reflexes: blocking Europe's moves toward free competition and resisting German-led efforts to democratize European institutions. He muffed his chance to tie the European knot quickly, before backlash against the short-term economic costs could unravel the process. That's what's happening now.

Mitterrand seemed paralyzed in dealing with Europe's new order

Mitterrand leaves the scene at a time of great self-doubt in France. The nation's economy is sinking, its role in Europe has weakened, and scandals are scarring the Establishment (page 58). But a few lessons can be drawn from his era. For one thing, 14 years is too long to rule a modern country: Longevity breeds corruption and kills purpose. Toward the end of his reign—the longest of any French ruler since Napoleon—Mitterrand said as much, though he wouldn't quit. A second lesson is that France should join global capitalism, not fight it. Oddly, French conservatives are just as guilty as socialists of state intervention.

As France bid *adieu* to its ex-President in a mass at Notre Dame cathedral, one message was clear: For all his faults, Mitterrand helped France shake off the ghosts of a divisive past. If France's new rulers still have a hope of keeping their country in the global power game, it may be largely thanks to the pragmatic politics of François Mitterrand.

Toy is BUSINESS WEEK's Paris bureau chief.

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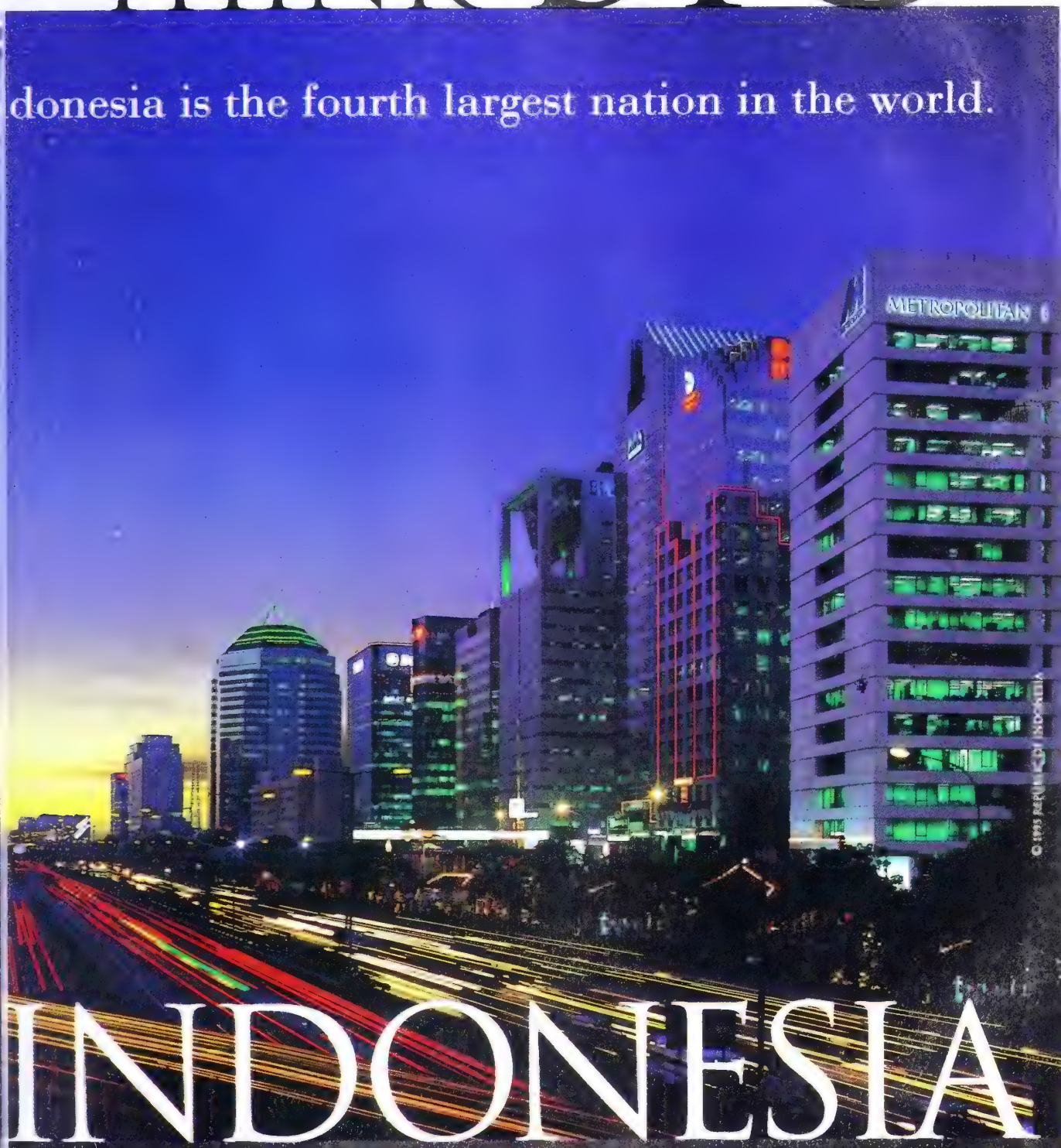

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MORE POWER TO INDIA

Why Enron renegotiated its deal–on Maharashtra's terms

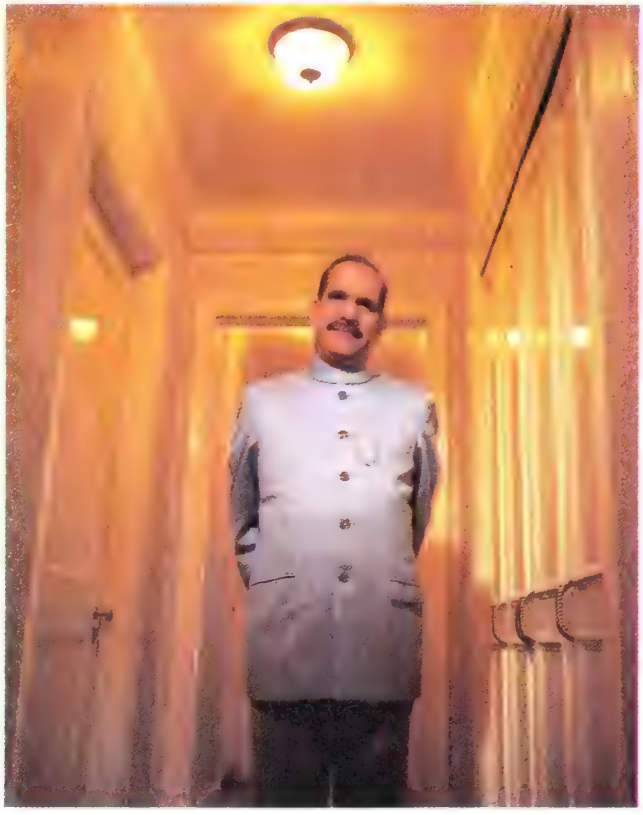
Did Enron Corp. blink? After months of bitter exchanges, the natural-gas and pipeline company and Indian negotiators agreed on Jan. 8 to revive the country's controversial Dabhol power project. Last summer, Maharashtra state's new chief minister, Manohar Joshi—who rode to power on a pledge to "drive Enron into the sea"—cancelled the project, citing padded costs and too high electricity rates.

Joshi now seems to have emerged as the biggest winner in the battle. The new deal he cut with Enron cuts the project's price tag 11%, to $2.5 billion, lowers the proposed electricity rates Enron can charge its customers, and makes a state-owned utility a new 30% partner of the project. The deal also increases the plant's output to 2,450 megawatts from 2,015, resulting in what Indian officials claim ranks among the lowest cost per megawatt in the country. "Maharashtra has gained tremendously by this decision," Joshi says.

One reason the Houston company may have given such a sweet deal is that it has more at stake in Dabhol than the power project. The $9 billion company has 29 global power and pipeline projects pending or under way in Bolivia, Brazil, China, and Turkey. Enron is also leading a $4 billion liquefied natural gas processing plant in Qatar that needs the Indian plant as a buyer for its fuel.

WIGGLE ROOM. Enron therefore sorely needed a Dabhol settlement to demonstrate that its global power strategy can't be easily derailed by local politics. "The facility looks a lot more secure as a project that will make money," says Donaldson, Lufkin & Jenrette Securities Corp. analyst Curt N. Launer.

It could also convince leaders of other developing nations that the company and its tough chief negotiator, Enron Development CEO Rebecca P. Mark, aren't as hard-nosed as they have seemed. Since Dabhol flared up, Mozambique officials complained of Enron's tactics in negotiating a gas-pipeline contract in that southern African country. "[Dabhol] has been such a publicly played-out wrangle that it has focused the attention of other governments," says Julia Nanay, a director at Washington-based energy consultant Petroleum Finance Co. The renegotiation prompted Enron to withdraw a suit seeking $500 million in damages from Maharashtra for the plant's cancellation.



UPPER HAND: *Joshi got a bigger plant at lower cost*

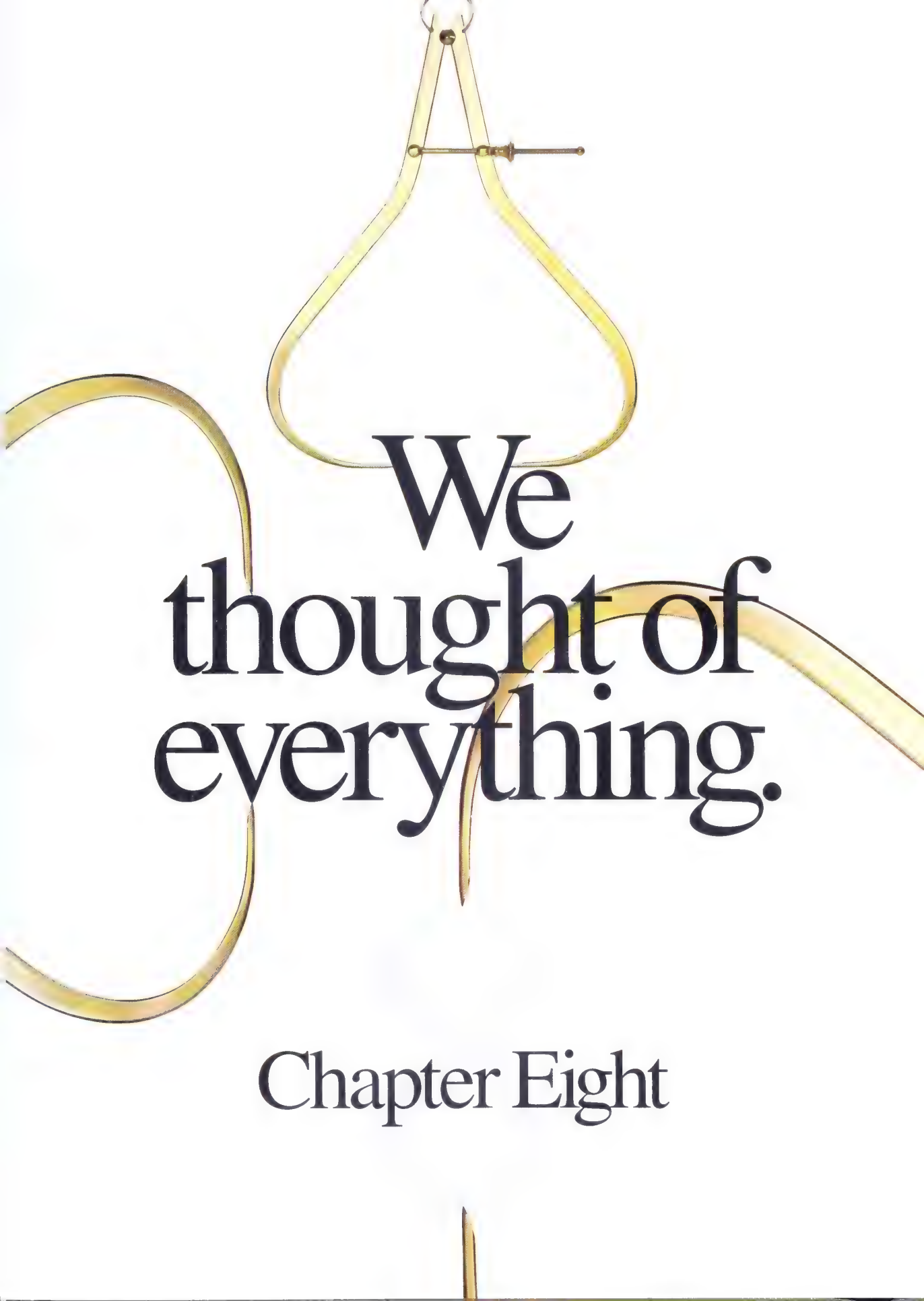
Enron gave up a lot to get the deal moving. In addition to building a more powerful plant for substantially lower electrical rates, it gave the state utility a voice in future decisions related to the plant. Upon cancellation, Enron lost a profit of $75 million from the sale of a 20% stake in the project to New Orleans-based utility Entergy Corp. Mark declines comment on the project's new expected rate of return, once estimated to be as high as 23%. However, the restructuring "makes it a very rational process for us and still provides very fair rates of return for our shareholders," says Mark.

For its part, India hopes to improve a tarnished reputation in the international business community, which viewed the contract repudiation as a dangerous shift. The cancellation of the project had been held out as a victory for the country's antiforeign Hindu nationalists. Being able to secure the deal on better terms is now hailed as a victory. "It's a great case study of how well India functions," says Ajay Shah, an opponent of the original agreement and president of a Bombay think tank. Although India has no regulatory framework for setting up utilities, he says, a second negotiation produced a deal at more favorable terms than an earlier one reached by members of Prime Minister P. V. Narasimha Rao's Congress Party.

Potential snags remain, but Mark says that they won't be major hurdles. Enron and Maharashtra must reach a new power-purchase agreement. Then lenders must approve the revised terms. Pending those approvals, construction could resume in 90 days, says Mark. She says anticipated savings in equipment costs in a second phase of the project will offset the lower electricity rates. "We're comfortable with the project," says Mark. With so much at stake in other dealings, the best course for Enron was to settle with India now—to ensure keeping on track elsewhere.

By Gary McWilliams in Houston, with Sharon Moshavi in Bombay

> Enron sorely needed a settlement in India to demonstrate that its global power strategy can't be derailed by local politics



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Chapter Eight

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POLAND: SO MUCH FOR KWASNIEWSKI'S HONEYMOON

Pink smoke bombs and a pig's head waved on a stick greeted the inauguration of Aleksander Kwasniewski as Poland's President on Dec. 23. A crowd of 1,000 or so marched through Warsaw, jeering his communist past. Outgoing President Lech Walesa refused to show up. Instead, he retreated to Gdansk in a huff, aiming to resume work as an electrician in the shipyards where he started the anticommunist revolution 15 years ago.

Before he left, Walesa tossed a bomb of his own. His outgoing Interior Minister, Andrzej Milczanowski, charged Prime Minister Jozef Oleksy—a Kwasniewski ally—with spying for Russia. Oleksy admits a friendly relationship of dinners and hunting trips with Vladimir Alganov, a Soviet intelligence officer in Warsaw from 1981 to 1992 but dismisses the espionage charges as a "dirty fabrication." But on Jan. 8 he began a short "holiday" while the chief military prosecutor and a special parliamentary committee probe the allegations.

"RED WEB." The Oleksy affair has dealt the slick 41-year-old Kwasniewski a severe setback. He had campaigned as a Polish JFK—a charismatic reformer and conciliator who could bridge the gap between Poland's bitterly divided political blocs. But now, "Poland is more divided than before the election," says political scientist Helena Bartnowska. Indeed, the spy charges have dashed Kwasniewski's plan to bring centrist leaders into his circle. Such figures, says an insider, are avoiding their phones. In a gesture of unity, Kwasniewski has even resigned from the Democratic Left Alliance (SLD), the leftist party he headed. But few are impressed.

Kwasniewski's handling of the affair has not helped. Instead of calling for Oleksy to step aside while being investigated, he kept quiet, adding to many Poles' fears that he's part of a "red web" crony system. "He damaged his efforts to prove he is President of all of Poland," says Andrzej Olechowski, the former Foreign Minister now running his own center-right party, Movement of 100. Oleksy made matters worse by firing a deputy interior minister working on the case and replacing him with an old chum.

KWASNIEWSKI: *The wrong move*

The political battling hasn't had time to hurt the economy, which is still chugging along at a 6% annual clip. The scandal may even have the effect of forcing Kwasniewski to toe the reform line—to ease local and foreign investors' suspicions. The President has made it clear that he intends to reform the pension system, rein in spending, speed up privatization, and push for membership in NATO and the European Union. He can deliver because the SLD dominates parliament.

HOT NEW MARKET. But the two sides have to be careful that the squabbling doesn't get out of control. Nasty election tactics, including Walesa's red-baiting, left Poles with a bitter taste. Now, the mudslinging is continuing as if the campaign wasn't over. The treasury, headed by an SLD minister, is saying Walesa owes back taxes on the $1 million he received from Warner Bros. in 1989 for the film rights to his life. For their part, Walesa supporters are hammering away at Kwasniewski's lies about his education and his refusal to disclose possible conflicts of interest with his wife's business activities. There's a risk that the cachet Poland has gained as a hot new emerging market could be tarnished.

What's certain is that former communists' efforts to look like responsible leaders of the future have been severely hurt. They are probably in for trouble in the parliamentary elections in 1997. Kwasniewski's best course is to make sure that the inquiry into Oleksy's actions is handled objectively from now on. Otherwise, his presidency could be crippled.

By Karen Lowry Miller in Bonn

GLOBAL WRAPUP

GERMAN PHONE FOLLIES

▶ Deutsche Telekom, the giant German phone monopoly, is suffering from a New Year's hangover. It has been blasted for mistakenly charging 11 million customers weekday rates on the holiday—which fell on Monday—rather than cheaper holiday rates. Customers are also in an uproar over plans to cut long-distance charges but raise local rates. There is even concern that these pratfalls could set back Chancellor Helmut Kohl's efforts to privatize the phone company. To atone, Deutsche Telekom will offer cut rates on the last Sunday in February.

TROUBLED TURKEY

▶ Turkey has been rocked by violence and political turmoil since last month's inconclusive general elections gave a big boost to Islamists. The most shocking incident came on Jan. 9, when gunmen killed two leading industrialists in an Istanbul office tower. The dead men, Ozdemir Sabanci and Haluk Gorgun, headed the local Toyota venture—the largest Japanese investment in Turkey. The Sabancis control one of Turkey's two most powerful business empires, including a 50% stake in the Toyota plant. The authorities are putting the blame for the attack on leftist guerrillas.

The political uncertainty seems likely to continue for some time. Necmettin Erbakan, leader of the Islamist Refah Party, which won the largest bloc in parliament, has been invited to form a government. But he is widely expected to fail, and a center-right coalition may eventually come to power.

EXECUTIVE SUITE

CHRYSLER'S MOST VALUABLE PLAYER?

Extending Bob Lutz's contract weakens Kerkorian's hand

In the battle for control of Chrysler Corp., President Robert A. Lutz is the wild card. Chairman Robert J. Eaton needs his product expertise and vision. Investors fret that Chrysler's stock would tumble without him. And disgruntled shareholder Kirk Kerkorian would love to lure Lutz into his camp.

Now, Chrysler's board may be trumping Kerkorian. On Jan. 4, Lutz told BUSINESS WEEK that the board had extended his contract for two years past Chrysler's mandatory retirement age of 65—until February, 1999. "Reports of my pending retirement," he says, "have turned out to be greatly exaggerated."

Chrysler officially declines comment, but insiders say keeping Lutz is crucial to prevailing over Kerkorian, who is gearing up for a spring proxy battle to put his top aide, former Chrysler Chief Financial Officer Jerome B. York, on Chrysler's board. Extending Lutz's reign diminishes concerns that Kerkorian has stirred up. Notes Theodore Shasta, an analyst at investment firm Loomis, Sayles & Co., a big shareholder: "Lutz is the guy that Wall Street loves."

"A PLUS." More than anyone else, Lutz is responsible for Chrysler's current success. The charismatic former fighter pilot revamped Chrysler's engineering ranks into nimble, cross-functional teams and championed daring styling to match the sporty performance of models such as the Dodge Intrepid sedan and Ram pickup. A string of popular models has boosted Chrysler's U.S. market share two points in the past five years, to 14.3%. Says one Chrysler exec: "Keeping Bob is a plus in the Kerkorian fight, but it's also a plus for the company overall."

It's hard to picture Chrysler without Lutz. The Cuban-cigar-wielding executive personifies Chrysler's image as Motown's brashest auto maker. His flamboyant, often combative personality probably cost him the chairmanship because of clashes with his previous boss, Lee A. Iacocca. But his blunt opinions and streamlined approach to product development make him a standout among Big Three execs. When he and Eaton introduced the new Plymouth Prowler earlier this month, Lutz curtly summed up his thoughts on critics of the retro-styled hot rod: "If some people don't like it, well, we just don't care."

Eaton, whose image is decidedly lower-key, calls Lutz "integral to our success." Against long odds, the two have established a close working relationship. In March, 1992, after Eaton left General Motors Corp. and beat out Lutz to succeed Iacocca, all of Detroit expected Lutz to quit. Instead, he and Eaton bonded because of their love of fast cars—and a shared wish to see Iacocca retire on schedule. Eaton approved the company's five-year product plan and gave Lutz free rein to execute it.

Lutz embraced the chance. "I have an unusual ability to direct the product-creation process, sort of a gift," he says. "I'm much like the conductor of a symphony orchestra." In 1989, he and engineering exec François J. Castaing created Chrysler's vaunted "platform teams," which organized engineers around specific models. The teams were later expanded to include marketing, manufacturing, design, and financial staffers.

Tearing down walls between the groups made product development faster and cheaper and unleashed staffers' creativity, leading to better-looking, better-performing vehicles. Creating the teams "was a total 180-degree turn," says Robert S. "Steve" Miller Jr., formerly Chrysler's chief financial officer and now CEO of Morrison Knudsen Corp. "[Lutz's] product vision was different from anything we had seen before."

Even York concedes that Lutz, whose total compensation came to $4.6 million in 1994, "is arguably the best product-development executive on a worldwide basis." Nonetheless, Kerkorian & Co. hold Lutz and Eaton accountable for

When Kerkorian's can started praising Lutz last fall, they were wid seen to be courting hi Lutz says he "never even considered" switching sides

ROBERT A. LUTZ

FEB. 12, 1932 Born in Zurich, the son of a Swiss banker

1943 Became a U.S. citizen when his parents were naturalized

1954–59 U.S. Marine Corps pilot

1959–62 Earned BS and MBA at the University of California at Berkeley

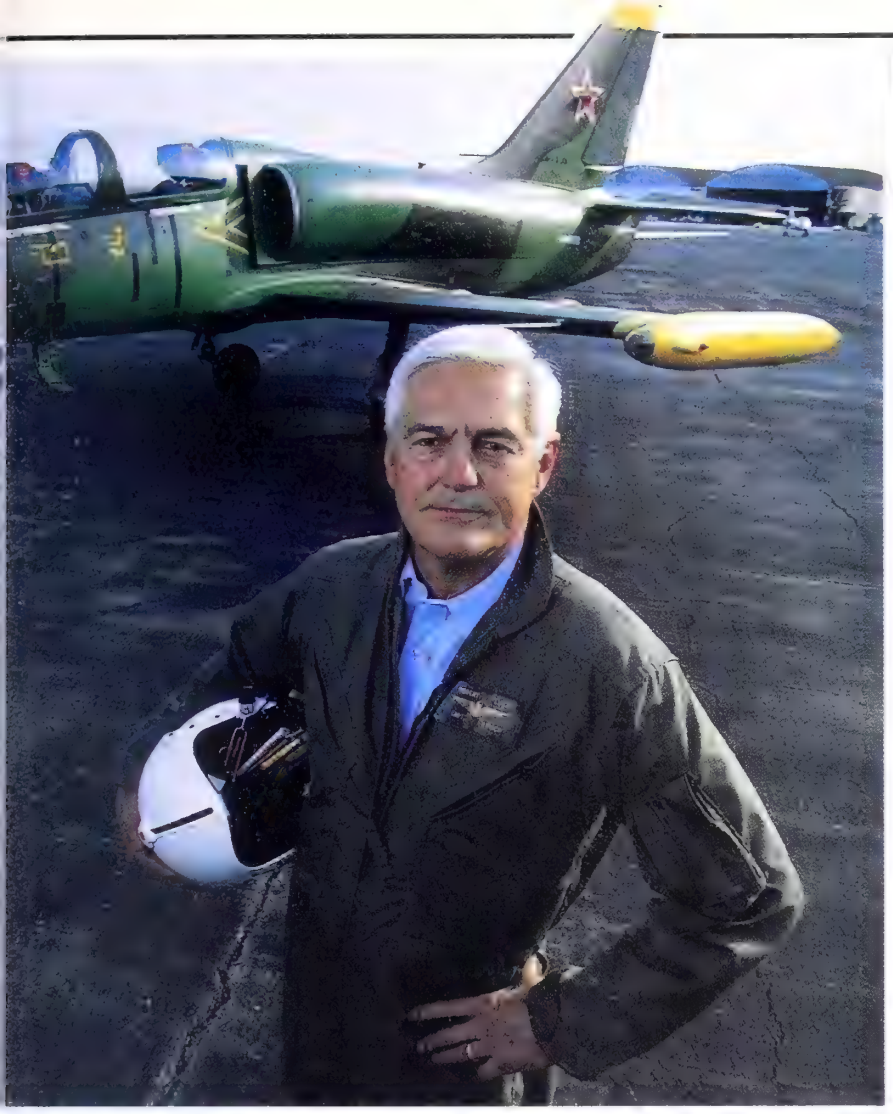
1963–71 Joined General Motors as a product planner. Eventually promoted to head of sales and marketing at Opel unit in Germany

1971–1974 Executive vice-president of sales and director, BMW in Munich

1974–86 Joined Ford Motor as chairman of German operations. Rose to head international operations

1986 Joined Chrysler as executive vice-president and director

1991 Named Chrysler's president



TOP GUN: *Lutz pilots his 600-mph Albatros jet fighter on weekends*

what they say is Chrysler's chief failing—spotty quality. Although some of Chrysler's trucks rank near the top in J. D. Power & Associates Inc.'s 1995 quality survey, its cars rank below the industry average. Since 1991, Lutz has overseen day-to-day operations that have the greatest impact on quality.

Lutz has long contended that the quality gap between Chrysler and industry leaders Honda Motor Co. and Toyota Motor Corp. is insignificant. But consultants and analysts say he hasn't used his clout to stamp out defects. And Lutz admits that Chrysler needs to put "tremendous focus" on improving quality.

It's just one conviction he shares with Eaton. And when the two Bobs don't agree, they hash out their differences in private. Lutz, for example, wanted to announce the Prowler months before its Jan. 3 introduction. When Eaton overruled him, saying Chrysler too often alerts rivals to upcoming products, Lutz accepted the decision amiably. "If we're at loggerheads, it's always strictly business," he says. "It never gets personal."

Such congeniality is a far cry from the state of war that prevailed between Lutz and Iacocca. Lutz often ridiculed Iacocca's sense of style and mimicked him maliciously. In 1991, when Iacocca was exploring a merger with Fiat, Lutz argued loudly that Chrysler should go it alone. After the talks fell apart, he told reporters: "You really can't find a husband for a woman who is sick on her deathbed in the hospital."

Just five years later, Chrysler is remarkably robust. Insiders say Lutz hated the thought of retiring on schedule, in February, 1997, because he's reveling in the turnaround. When York publicly praised Lutz last fall, he was widely seen to be courting him. But Lutz says he "never even considered" switching sides. That's not to say Kerkorian's interest didn't prompt the contract extension. "Some of the things the other side had to say put Bob in a pretty good position around here," says one Chrysler exec.

It's a position he traveled a long and storied road to reach. Born in Zurich in 1932, Lutz moved to New York City as a child when his father, a banker at Credit Suisse, was posted there. He became a U. S. citizen at 11. Because he switched schools and continents repeatedly, he didn't finish high school until he was 22. But along the way, he mastered English, French, and German—and enough Italian to coach a Siena bartender on making a dry martini.

Captivated from an early age by motorcycles, cars, and planes, he headed for the Marine Corps intent on becoming a fighter pilot. After flying jets for five years, he moved to California in 1959 and later earned a BS and an MBA at the University of California at Berkeley.

Then began his fast ride through the auto industry. A Ford Motor Co. recruiter wooed him first, but Lutz's father prevailed on an acquaintance, Fred Donner, then chairman of GM, to give him an interview. Lutz was hired as a planner. Two years later, he went to GM's German unit and quickly rose to executive vice-president for sales and marketing. In 1971, he moved to BMW as marketing director. Three years later, he went to Ford's European operations, where he shot up the ranks, becoming head of Ford of Europe Inc. in 1979. In 1982, he returned to the U. S. as executive vice-president for international operations.

A POTHOLE. Then came a brief stumble. Ford's European business abruptly plummeted, and many insiders held Lutz responsible. He was sent back to Europe to fix the problem, and when he returned to Dearborn two years later, he was sidetracked to head Ford's sleepy truck operations. From there, Iacocca plucked him to join Chrysler as an executive vice-president in 1986. He became president in 1991, but his relations with Iacocca were already souring.

Lutz's enthusiasm for high speed has never faded. He owns a dozen cars and five motorcycles and a hulking Lamborghini V-12 engine sits on the floor of his office. Lutz often pilots his McDonnell Douglas Corp. helicopter from his nearby Ann Arbor home to Auburn Hills. His daredevil persona was etched in Motor City history when he crash-landed another copter in 1991, walking away with minor injuries. His latest toy is a Czech-made L-39C Albatros jet fighter. On weekends, Lutz and his third wife, Denise, streak across the Michigan sky at nearly 600 miles per hour—a pastime that led a Detroit TV station to dub him "Chrysler's top gun."

While he hasn't achieved his dream of holding the top spot at one of the Big Three, Lutz knows he's wanted at Chrysler into 1999. For Chrysler's rivals—and for its best-known shareholder—the prospect of Lutz staying on for three more years can't be a comforting thought.

By Bill Vlasic and David Woodruff in Detroit

Cover Story

SCOTT McNEALY'S RISING SUN

How he's taking the computer maker to new heights

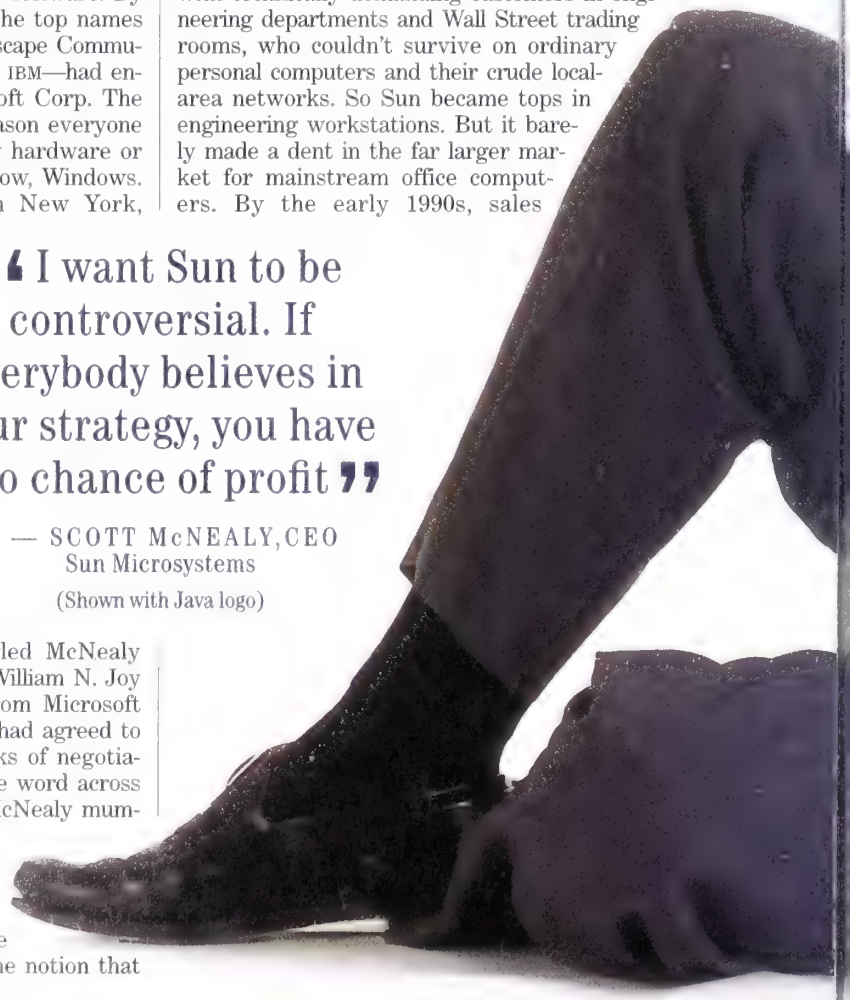
Scott McNealy was dog-tired. For weeks, the chief executive of Sun Microsystems Inc. had been sealing deal after deal for Java, Sun's red-hot Internet software. By the first week in December, a bunch of the top names in computing—everyone from Internet star Netscape Communications to database kingpin Oracle Systems to IBM—had endorsed Java. Everyone, that is, except Microsoft Corp. The software giant was holding out for the same reason everyone else was so excited: Java programs run on any hardware or operating system, bypassing Bill Gates's cash cow, Windows.

After three frenzied days of meetings in New York, McNealy was looking forward to a full night's sleep. All the schmoozing—including talks with IBM CEO Louis V. Gerstner Jr. that had yielded a promise by the world's biggest computer maker to use Java—was taking its toll. And back home, McNealy's 4-week-old firstborn had been cutting into his shut-eye. The following day, Dec. 7, would be another marathon: an interview at CNBC, customer meetings, and a trip home on the leased corporate jet in time for a business dinner—and a San Jose Sharks hockey game.

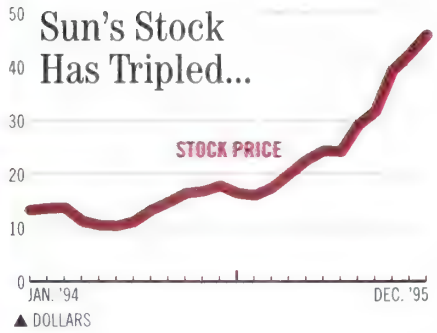
NO LIGHTWEIGHT. At 2 a.m., the phone in his room at the Grand Hyatt jangled McNealy awake. It was Sun co-founder and Javameister William N. Joy with big news: Joy had just received a fax from Microsoft Senior Vice-President Roger Heinen. Microsoft had agreed to license Java on Sun's terms—ending four weeks of negotiations. Time to uncork the bubbly? Or spread the word across the Net? No way. Chronically sleep-deprived, McNealy mumbled, "Great job," and rolled over.

Correction: incredible job. Microsoft's capitulation stands as a defining moment for Sun and its 41-year-old CEO. For more than a decade, McNealy has shouted himself hoarse preaching the gospel of network computing—the notion that you begin to realize the true value of computers only when they work together in networks. The message worked well with technically demanding customers in engineering departments and Wall Street trading rooms, who couldn't survive on ordinary personal computers and their crude local-area networks. So Sun became tops in engineering workstations. But it barely made a dent in the far larger market for mainstream office computers. By the early 1990s, sales

> "I want Sun to be controversial. If everybody believes in your strategy, you have zero chance of profit"
>
> — SCOTT McNEALY, CEO
> Sun Microsystems


(Shown with Java logo)

With its core business generating record earnings and the Internet boom and the frenzy over Java adding fuel, Sun's stock has hit new highs. But the always competitive McNealy, who likes to use his stock price to keep score against competitors, figures it can do better. His goal: $100 in 1996.



...But It Lags Other High-fliers

PRICE-EARNINGS RATIO	
NETSCAPE	371.0
ORACLE	28.4
MICROSOFT	25.0
SUN	15.8

Estimates for current fiscal year

DATA BLOOMBERG FINANCIAL SERVICES, ZACH'S INVESTMENT RESEARCH

slowed, profits dropped, and it seemed the company would never break into the big time.

That, however, was before the Internet explosion and Java. With businesses tripping over themselves in the past 18 months to get on the Net, Sun's mantra—"The Network is the Computer"—has begun to resonate around the globe. Even the mighty William H. Gates III—whose software dominates the huge PC market—concedes that McNealy's Sun has the right stuff for the next era of computing.

That Sun now finds itself in the center of the computing universe has a lot to do with the unlikely character at the top. The toothy, boyish-looking McNealy has an unusual résumé in an industry driven by technical whizzes and creative entrepreneurs. Unlike Gates or Steven P. Jobs, he didn't drop out of college to answer the call of the burgeoning PC business. Nor did he work his way up through engineering, as did Intel Corp.'s Andrew S. Grove and dozens of other Silicon Valley execs.

You won't find McNealy sweating over computer code down in the engineering lab. He studied economics at Harvard University and got his MBA at Stanford. His passions are hockey and golf. And he's famous for sophomoric pranks and shoot-from-the-lip one-liners. Typical of his wit is this assessment of Microsoft's Windows and MS-DOS: "whipped cream on a road apple."

But McNealy has proved to be anything but a lightweight. Indeed, while CEOs with better technical credentials have flamed out—flitting from one techno-fad to another or neglecting the fundamentals of the business—McNealy has emerged as one of the

Scott G. McNealy

TITLE CEO, Sun Microsystems
VALUE OF SUN STOCK Over $200 million
BORN Columbus, Indiana, 1954
EDUCATION BA, Harvard; MBA, Stanford
JOB HISTORY
- Worked in manufacturing at Rockwell Corp. after Harvard and at FMC after Stanford
- Directed manufacturing at Onyx System for 10 months, 1980–81
- Joined Sun in 1982 to head operations
- Became CEO in 1984

FAMILY Married; son, Maverick, born Nov. 7, 1995
FAVORITE FOOD Pizza (double cheese)
FAVORITE BEVERAGE Bud Light
CAR Cadillac STS
HOBBIES Sun, hockey, golf, Sun
PET PEEVE Ties
MOST HATED ADJECTIVE APPLIED TO HIMSELF Bra
MOTTO Have lunch, or be lunch
MOST ADMIRED PERSON Newt Gingrich–"He makes me look like a diplomat"
MEMORABLE ACTIONS
- Lured $40 million account away from arch rival Apollo in 1983, putting Sun on the ma
- Took on Intel in 1987 with SPARC micr processor
- Took on Microsoft in 1995 with Java Internet software

A SON FOR SUN'S CHIEF: *McNealy, at home with 2-month-old Maverick and dog Network, says Sun still comes first*

Valley's most respected managers. Programmer-turned-entrepreneur Lawrence J. Ellison, CEO of Oracle, salutes McNealy's blend of talents. "There are two things I think about Scott," says Ellison. "One is passionate leadership, and the other is his rigorous financial management. And that's uncommon to find in one person. Usually, the financial guys aren't so outspokenly passionate, and all leaders are not detail-oriented."

Those talents, plus a killer competitive instinct and nonstop drive, have kept Sun on course through a decade of wrenching change in the computer industry—while IBM stumbled and new leaders such as Intel and Microsoft emerged. Now, Sun has a shot at the leadership in the network era.

***TOY STORY* GLORY.** As McNealy has long predicted, the network has won. The typical stand-alone PC, he insists, has been a complex time-waster, a "hairball on the desktop." Now, thanks largely to the Net, consumers and businesses have come around to Sun's view: When computers are networked, their power multiplies geometrically. Not only can people share all that information inside their machines but they can reach out and instantly tap the power of other machines—essentially making the entire network their computer.

Sun didn't exactly invent network computing, but it can claim to be the only pure play in the business. The two technical forces behind Sun—co-founders Bill Joy at the University of California at Berkeley and Andreas V. Bechtolsheim at Stanford—had been computer-science students at a time when many of the networking technologies that formed the basis of the Net were created. They built that technology into Sun's first computers in 1982 and into every Sun machine since.

Now, all this is paying off. Already, approximately 35% of all the World Wide Web servers in the world are Sun machines. And as companies adopt Internet standards for internal networks, they are turning to Sun. Federal Express, Gap, AT&T Universal Card Services, and Charles Schwab all use Sun networks. And thanks to the new UltraSPARC chip, Sun's workstations are once again on the leading edge. Sun machines recently stole some of Silicon Graphics Inc.'s Hollywood pizzazz by helping to create the blockbuster movie *Toy Story*.

In Sun's first fiscal quarter ended Sept. 30, earnings jumped 120%, to $85 million. That followed an 82% hike in fiscal 1995, to $356 million, on a 26% jump in revenue, to $6 billion. Sun's stock tripled, from 16 to 45¾ since last year, adjusted for a 2-for-1 split on Dec. 12. But like other technology companies, Sun's stock has been giving back recent gains, plunging 6.8% on Jan. 9, to 37¾. Typically, McNealy isn't satisfied, complaining that other companies—including newcomer Netscape—rate higher price-earnings ratios. His New Year's resolution: a $100 stock price by yearend.

Pretty heady stuff. "We're all having a blast," McNealy says. But nobody's goofing off, least of all McNealy. He's painfully aware that this golden moment will soon pass. "I just wish I didn't have to sleep," he says.

In the meantime, Sun still faces big challenges. For one, despite the buzz about Java, the company still has to figure out how to make it a business (page 73). And there's a downside to the triumph of Sun's network vision: Every computer maker now shares it and is gunning for Sun. At the same time, Intel and Microsoft continue to push PC performance into workstation territory, and Sun's workstation rivals are

ANIMAL HOUSE ANTICS: *Frat-like high jinks, such as this squirt-gun war, help McNealy (left) to bond with and energize his staff*

McNealy has strong views and needs to listen better, but his stubborn belief in Java has made Sun red-hot

coming on strong. What's more, the company's ascent into the top tier of computer makers puts new demands on Sun. In addition to pumping out killer hardware and software, it also must cater to the needs of big customers—the way rivals IBM, Hewlett-Packard, and Digital Equipment long have done.

That's why, after a short Christmas break with his family—his wife of 16 months, Susan, and son, Maverick (the name will be redundant, boasts Dad)—McNealy is back to his 80-hour weeks and heavy travel schedule. "We have too much work to do," he says.

Besides, he loves the pace. In fact, he was born to it. His father, R. William McNealy, was vice-chairman of American Motors Corp. By the time he was a teenager, Scott was spending evenings with his dad, poring over AMC memos and golfing in foursomes with such industry luminaries as Lee A. Iacocca. Scott says he saw how AMC was marginalized because it never had sufficient market share—and he has vowed to make sure that doesn't happen to his company.

At Cranbrook Kingswood School, a prep school north of Detroit, McNealy emerged as a leader, captaining the tennis team. At Harvard, he became interested in economics—thanks in part to class section leader William J. Raduchel, who would later become McNealy's chief information officer and corporate development chief at Sun.

But McNealy was not a standout student. He was rejected from both Harvard and Stanford business schools—three times from Stanford. So he took a job as foreman at a Rockwell International Corp. plant in Ashtabula, Ohio, in 1976. The company was rapidly building truck hoods in expectation of a strike. The grind was so hard—two months of 14-hour days—that McNealy says it led to a bout of hepatitis that kept him hospitalized for six weeks.

"KIND OF A GOOF-OFF." When he finally did get into Stanford, his study habits and choice of curriculum didn't scream "CEO material." For one thing, he focused on manufacturing at a time when finance was the route to the top. Moreover, classmates say McNealy preferred playing golf to attending classes. "He was kind of a goof-off," says Curt Wozniak, a Stanford buddy and former Sun engineering vice-president. McNealy says he just didn't bother attending classes that he didn't think would help him get a job. "I minimized hours per grade point," he boasts. After graduating, he took undistinguished manufacturing jobs at tankmaker FMC Corp. and minicomputer maker Onyx Systems.

In those days, McNealy seemed determined not to pursue his dad's CEO quest. He once vowed never to work as hard as his father: That workaholism eventually led McNealy's parents to divorce. Instead, McNealy dreamed of running a small machine shop he could give to his kids and retiring early.

Then, in 1982, came the call that would change McNealy's fate. Former Stanford classmate Vinod Khosla asked McNealy to join him and computer designer Bechtolsheim in starting Sun. McNealy's manufacturing skills enabled the young company to keep up with wild demand as sales soared from $9 million in 1983 to $39 million in 1984. McNealy says he got manufacturing humming so well that soon he wasn't getting enough orders to sop up production. So he started running sales. But the new orders outstripped the cash available for expansion. So McNealy was tapped to look for help—and he settled on customer Eastman Kodak Co.,

SUN: JACK OF ALL TRADES, MASTER OF...THE UNIVERSE?

Sun's network computing is finally coming true, and now everybody is doing all the things Sun does

PRODUCT	REVENUE	STATUS	COMPETITORS
WORKSTATIONS	$2.7B	Sun has lost ground to Hewlett-Packard but is coming back with new UltraSPARC machines	HP, IBM, Silicon Graphics, Digital Equipment
SERVERS	$1.3B	This is Sun's way into corporate computing and its biggest Internet-related business so far	HP, IBM, Silicon Graphics, Compaq, Digital Equipment
SERVICES	$885M	Unix and networking-consulting opportunities are growing, but so is the competition	EDS, IBM, Oracle
SOFTWARE	$395M	Sun's Unix operating system is the most popular, but it hasn't sold well on non-Sun hardware	Microsoft, IBM
SPARC TECHNOLOGY	$99M	Sun's SPARC chips are now back on the leading edge, but Intel's Pentium Pro is a potential low-cost threat	IBM, Digital Equipment

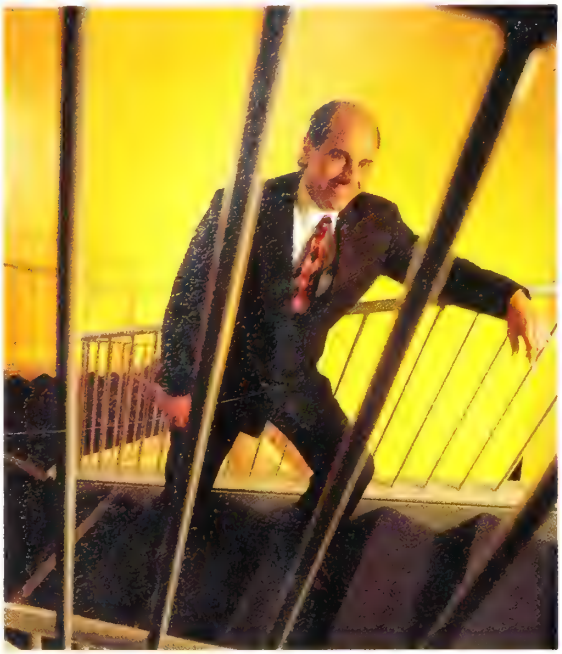
DATA: SALOMON BROTHERS INC., BUSINESS WEEK

DOUG MENUEZ/SABA

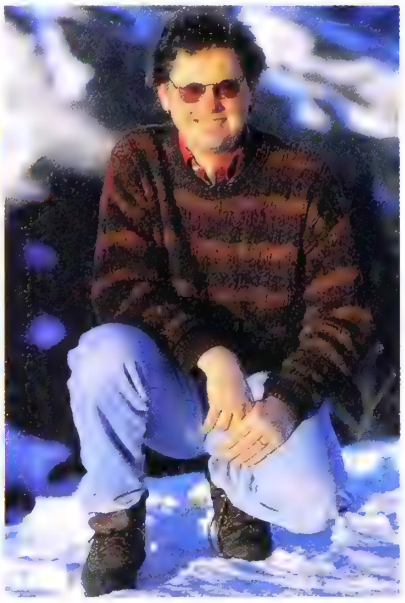
McNealy's Brain Trust

which was using Sun workstations in a microfilm project.

McNealy's tenaciousness and quick thinking impressed J. Philip Samper, then executive vice-president at Kodak. As a condition of investing $20 million, Kodak insisted McNealy take over as president in 1984. Samper later served as president of Sun's hardware unit. At about the same time, then-CEO Khosla left in a dispute with the board, so McNealy was appointed president, at least until the board found someone with more experience. But Sun's fortunes rocketed, and the directors stopped looking for a replacement. At 30, McNealy was officially named CEO.



SPARC PLUGGER: *Zander is president of Sun's hardware unit and the company's key marketing executive*



JAVAMEISTER: *Co-founder Joy is Sun's networking guru and now chief of Java*

DETAIL MAN: *Raduchel, the chief information officer, keeps Sun running–on its own machines*

McNealy soon etched his image on the industry. Although he says he dislikes being described as brash—his tag in dozens of newspaper and magazine stories—brash he was. In 1987, Sun joined with AT&T to develop a new version of the Unix operating system. IBM, DEC, HP, and other computer makers struck back by forming the Open Software Foundation to create another version of Unix. Never mind that these were the biggest companies in the industry and Sun was a relative upstart. McNealy publicly mocked OSF and its members, roaring that the initials really stood for "Oppose Sun Forever."

At Sun's Mountain View (Calif.) headquarters, he was building a corporate culture based on his own motto: "Kick butt and have fun." The company has become equally famous for its aggressive marketing and the juvenile antics staged around its headquarters. Each April Fools' Day, scores of photographers now arrive to record the elaborate pranks Sun engineers play on McNealy and other execs. Once, the company's engineers built a golf course hole in McNealy's office, complete with green and water hazard.

McNealy likes to join in the high jinks, too. He has played general at an intramural squirt-gun war. Last May, at a conference in San Francisco, McNealy spent a half-hour earnestly laying out Sun's vision for 4,000 computer buyers and programmers. Then he set out several cardboard fire hydrants bearing the names of rivals and introduced Network, a Greater Swiss Mountain dog that stars in Sun's ad campaign. Sure enough, McNealy led the dog to the hydrants and exhorted him to raise a leg. Network, evidently more tactful than his master, declined.

The humor, which is turned on everybody, including McNealy himself, has an important effect: It binds the company and helps employees live with their demanding jobs. "His humor and ability to raise a crowd to its feet is in many respects exactly what you need in CEOs and leaders of today's industry," says Thomas J. Meredith, a former Sun treasurer and now vice-president for finance at Dell Computer Corp. McNealy's special gift, says former sales vice-president Carol A. Bartz, now CEO of Autodesk Inc., is to energize his people. "Energy comes right out of his pores," she says.

NEWT BOOSTER. These days, McNealy tries to channel some of that energy to his new family. In addition to Susan and Maverick, the family now includes Network, McNealy's own Greater Swiss Mountain puppy. Although his compensation hit $3 million last year and the 2.9% of Sun shares he owns is worth over $200 million, McNealy remains firmly planted in the three-bedroom house he bought in the hills north of the Valley in 1986, although he owns a condo in Palm Springs. He still likes nothing better than playing hockey and is on two league teams so he can always find a game. Whether it's on the ice or the links, McNealy is determined to win. "It's just not in my nature not to be competitive," he concedes.

For socializing, he likes to barbecue and sit around with friends, drinking domestic beer and watching a hockey game on TV. Says Dick Boyce, a Stanford mate and PepsiCo Inc.'s chief financial officer: "He would be happy to be described as Joe Six-Pack working hard to get the job done."

His politics, however, are anything but mainstream. He's a libertarian, who has been known to rail against all forms of government regulation and the welfare state, and he's a big

Is Sun too preoccupied to focus on service? "They're grabbing at everything," says a Lockheed manager

fan of Newt Gingrich. That's unusual in Silicon Valley, where top executives turned out for Bill Clinton, but it doesn't stop the affable McNealy from mixing with other Valley notables. Lately, in fact, he has been spending time with Steve Jobs—Laurene Jobs and Susan McNealy met at an engagement party for McNealy given by Ellison. Now, the two families—both have infants—get together occasionally for dinner.

Almost nothing, however, takes McNealy away from Sun for long. "There was full disclosure" about that before the wedding," he says. "I'll never know my kids as well as most people," he adds wistfully. "But I've also got 15,000 people and $7 billion worth of market value counting on me."

Sun is not a one-man show. "One thing Scott has done is he has supplemented his leadership with some wonderful people," says Ellison. "You don't find Scott surrounded by dummies. You find Scott surrounded by real smart people, like Bill Joy and Eric Schmidt [chief technology officer] and others who do wonderful work." Those others include Edward J. Zander, president of Sun's hardware unit and the key marketing executive, and Raduchel, who as chief information officer is responsible for getting the company to run on its own machines.

To make the growing organization more nimble, in 1991, McNealy split Sun into seven "planets"—for hardware, software, service, etc. The setup got off to a rocky start because of turf battles among executives. Finally, in the summer of 1993, the CEO issued an ultimatum, says Schmidt: "Sign up, or get the hell out." Now, McNealy says his managers still aren't getting along as well as they should, but at least they're no longer fighting over who sells what.

SKATING WITH SHARKS: *His love of hockey led McNealy onto the ice with San Jose in a 1992 prank*

> "It's just not in my nature not to be competitive"

Concerned about his effectiveness, McNealy recently hired a "CEO coach," Chuck Raben of Delta Consulting Group Inc. Raben polled Sun managers on where the boss could improve. The consensus: McNealy, who admits he has an opinion on everything, needs to listen better. Raben gave McNealy a cheat sheet, reminding him, for instance, to make sure he has covered all the points raised in meetings with managers.

Still, Sun's execs don't want McNealy to change too much. "Management is always contentious at Sun," says Raduchel. "Conflict-free management is always a disaster."

A POST-WINTEL ERA? And nobody wants McNealy to abandon his strong opinions. After all, the Java technology that has made Sun the darling of the Web exists today in large part because of McNealy's stubborn belief in it. In late 1990, McNealy asked a departing engineer, Patrick Naughton, to take a last moment and write a memo on how Sun could improve. Naughton suggested creating a software system for portable devices—and McNealy persuaded him to stay and do it.

McNealy gave the project, code-named Green, total independence and served as its cheerleader. Once, with the team burning out, he dropped in for a demo. It was a shaky prototype, but the boss turned morale around when he exclaimed: "This is the greatest thing I've ever seen," Naughton recalls.

Eventually, Green dead-ended with projects for interactive-TV set-top boxes and personal digital assistants. But even as Green wound down, says Naughton, now vice-president for technology at multimedia startup Starwave Corp., "Scott salvaged a lot of things"—one of them Java. Says pal Steve Jobs: "When he believes in a strategy, he will stick with it through thick and thin."

An example of that is McNealy's determination to continue to do it all—chips, software, hardware, the works. That has been increasingly risky as off-the-shelf commodity technology has swept the market. But McNealy is convinced that the Net—and Java, in particular—will alter the dynamics of the business. "Applets" written in the Java language can be zapped across the Net to run on any device that has a Java "virtual machine"—a tiny bit of code that mimics a computer. If Java catches on big, the software lock-in of the Microsoft Windows/Intel (Wintel) design will end, McNealy says. Then, computer and software companies will once again be able to differentiate their products. Indeed, they'll have to. "If you're going to make automobiles, you have to make your own engine," he says.

Before that post-Wintel era arrives, McNealy has plenty of other battles. HP, IBM, DEC, and Silicon Graphics are all gunning for Sun's core computer business. HP claims to have stolen workstation business from 35 Sun customers since 1993 by offering what Sun concedes is superior service and support of big customers. "They're losing in workstations, playing catch-up in servers, and have lost their lead in the overall Unix market," says HP Senior Vice-President Willem P. Roelandts. Some customers worry that Sun has too much on its plate to focus on service deficiencies. "They're grabbing at everything," says Stephen W. Butt, a manager at a Lockheed Martin Corp. unit that switched to HP workstations.

Sun has beefed up its $885 million service and support unit, and upped the head count 50%, to 3,000 since 1994. McNealy, who calls on customers whenever he can, keeps close tabs. At Schwab, for instance, he checks in every six weeks or so. "Scott has followed up religiously," says CIO Dawn Lepore.

It's worth the effort. Commercial computing accounts such as Dunlop Tire Corp., which used Sun servers to replace mainframes, now make up a third of Sun's revenues. And the servers they buy help the bottom line: While growth in the workstation market has slowed and margins have contracted, the higher profits from servers have helped Sun boost its corporate gross profit margin to 44% for the

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first quarter, ended Sept. 30, from 41% in fiscal 1994.

By the end of 1996, Sun may find it more difficult to get such profits from hardware. That's because of Intel's next-generation Pentium Pro chip. PCs that use it will rival workstations in power. Worse, Intel has a four-chip "motherboard" that will let companies such as Compaq Computer Corp. crank out servers costing a quarter as much as Sun's midrange machines. "Intel servers will be the dominant servers on the Internet," predicts PaineWebber Inc. analyst Stephen K. Smith.

McNealy's answer, again, is Java. Once the new software succeeds in undoing the Wintel lock, customers will see how outstanding Sun hardware and software are, he argues. "Java opens up a whole new world for Sun," he says.

This view of the future is not a universal one. Despite all the excitement, Java is unlikely to transform computing overnight. First, there are security issues raised by a system of distributing software on the Net. And for now, the Java programs run slowly. "Java is still radically immature," says independent software consultant Mark Pesce.

This bothers McNealy not a bit. "I want Sun to be controversial," he says. "If everybody believes in your strategy, you have zero chance of profit." McNealy does fret that with so much on his plate, he'll be blinded to the next big thing: "We're so frantic with everything going on right now that we're missing something." This season, though, there's little danger of a solar eclipse.

By Robert D. Hof in Mountain View, Calif., with Kathy Rebello and Peter Burrows in San Francisco and bureau reports

NOW, SUN HAS TO KEEP JAVA PERKING

How hot is Java? Even before the official Jan. 12 release of Sun's bold new network software, 14 big-name companies, from Microsoft and Netscape Communications to IBM and Toshiba, have already agreed to license it for at least $125,000 a pop. As a result, Sun is years ahead of its original (admittedly modest) business plan—and scrambling to forge a new one. That's why on Jan. 9, Sun hired Alan E. Baratz to run JavaSoft. Says the former chief executive of Delphi Internet Services Corp.: "I probably won't be sleeping in the next couple months."

Baratz, once a top networking strategist at IBM, will have to be alert to keep Sun ahead of its own creation. A new computer language, Java lets programmers write tiny applications that can zip across the World Wide Web and bypass Microsoft's Windows when they arrive. Already, programmers have used Java to create some 600 "applets" for everything from animation to transmitting electronic "ticker tape." And because Java will be built into the next release of Netscape's Web browser, millions of personal computer owners will be sipping the cyberbrew this year.

"THE NEW INTEL." What's in it for Sun? Lots—but licensing revenue may be the least of it. Java will pay off, says Chief Technology Officer Eric E. Schmidt, if all it does is stimulate demand for Sun's network hardware, software, and service.

Still, Java offers potentially huge revenue opportunities that Sun—facing more competition than ever on the hardware front—can't afford to pass up. Besides licensing fees, Sun's main source of Java revenue this year will be from software tools to help developers create Java programs. In March, Sun will release Workshop for Java, a $100 package it expects will appeal to more than 300,000 Windows programmers.

Beyond 1996, the plans get murky. For one, Sun is thinking of offering its own Java applets, including an Internet variation on Notes, Lotus Development Corp.'s groupware. But even if it convinces software partners that it's not stealing their business, Sun couldn't charge Microsoft-like prices because individual applets have far fewer functions than full traditional programs.

The biggest jolt would be a Java-based operating system that could replace Windows completely. Sun already has a prototype that could be ready by 1997, but company officials won't say whether they plan to market it. If they do, free or inexpensive distribution over the Internet could make it a standard almost immediately. Says Gartner Group analyst Hubert C. Delaney: "Java doesn't have to make money for Sun, just help them break Microsoft's business model."

A POTFUL OF DOLLARS? *For now, JavaSoft's Baratz may find income in licensing fees and software tools*

Sun isn't limiting its plans to computers. Schmidt envisions embedding the software that runs Java applets in everything from printers to wireless phones, giving them more computerlike adaptability. Sun may even design a microprocessor chip tuned to run Java applets at lightning speed. Says Schmidt: "This is a path to where Java could be the new Intel."

New Intel? New Microsoft? Whew. Nothing would make Sun Chief Executive Scott G. McNealy happier, but he'll be satisfied, he says, if Java simply gives Intel and Microsoft some competition—opening the market for Sun. That prospect alone has investors psyched: The day Microsoft endorsed Java, Sun's market value jumped $336 million. "The halo effect is stunning," says McNealy. Anything more will be cream in his coffee.

By Robert D. Hof in Mountain View, Calif., and John Verity in New York

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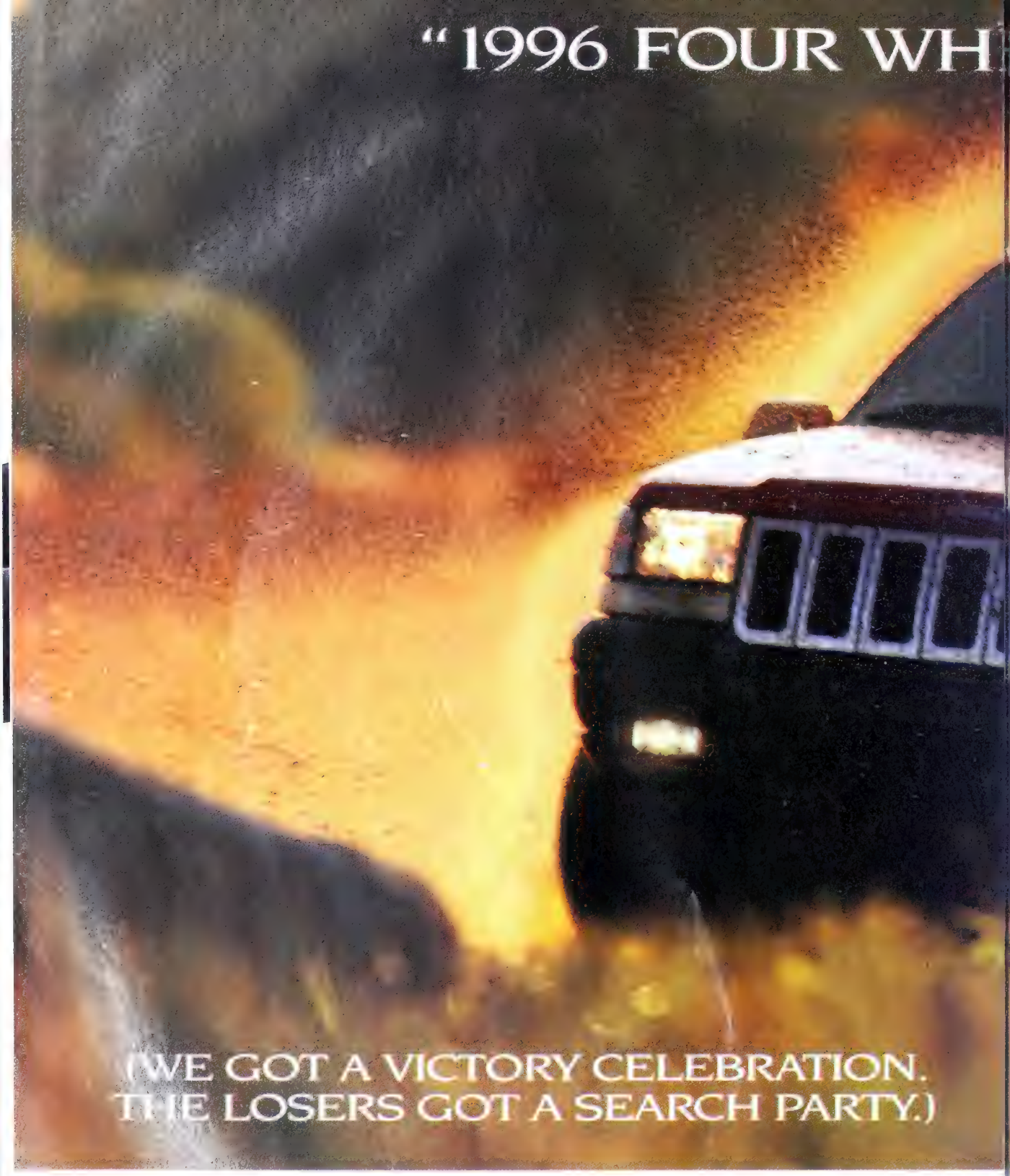

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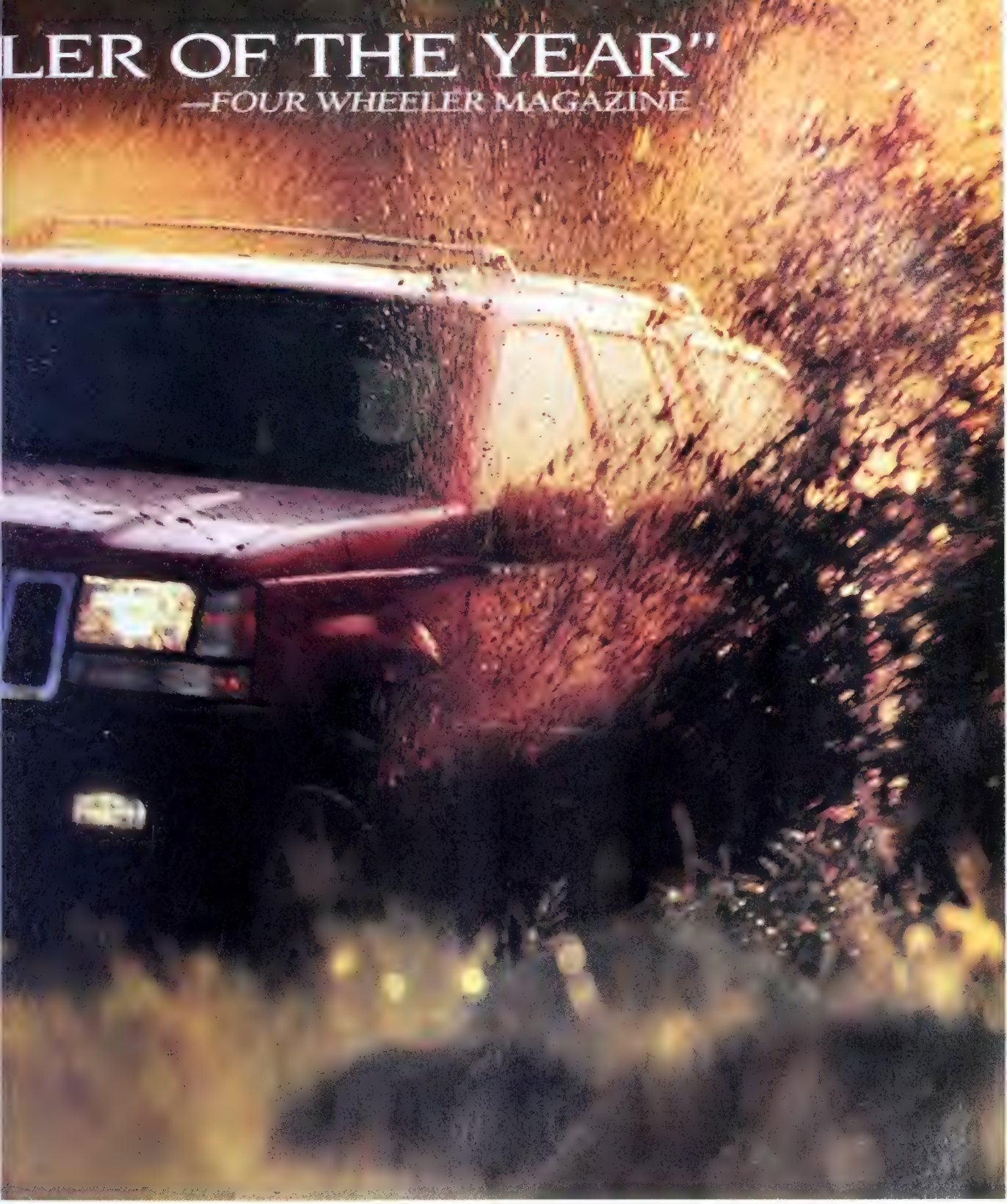

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BANKS

NEW MAN ATOP THE PYRAMID

Can CEO David Coulter replace BankAmerica's infighting with team spirit?

The message was clear. At an afternoon-long meeting on Jan. 3, just two days after taking over as chief executive of BankAmerica Corp., David A. Coulter laid down the law of his new administration to his top lieutenants: End the turf wars and office politics that long have been a major distraction at the nation's second-largest bank. Recalls Coulter, in his first interview as CEO: "I said, 'This is a team environment, and they have to be 100% committed.'"

BankAmerica, with $230 billion in assets, is a formidable institution despite the internal feuding. It has one of the best franchises in banking, with a balance of consumer and corporate businesses, and dominance in the fast-growing western U.S. market. Profits are on the rise, too. The bank earned nearly $2 billion in the first nine months of 1995, up almost 24% from the same period the year before.

CHANGE OF STYLE. Yet, partly thanks to the infighting as well as one of the industry's most ponderous bureaucracies, BofA lags more nimble competitors. Over the past four quarters, it earned $1.15 for every $100 of assets, compared with $1.59 and $1.83, respectively, for California rivals First Interstate Bancorp and Wells Fargo & Co. BofA's organizational problems sap the bank of energy and focus, BofA watchers say, handicapping it in the marketplace and damaging its financial results. Competition is becoming increasingly heated, and if BofA fails to deal effectively with those problems, its market position could be seriously eroded.

COULTER'S CHALLENGES

- Curbing political infighting and taming the bank's ponderous bureaucracy
- Improving BofA's middle-of-the-road financial performance
- Positioning BofA to capitalize on the rapidly changing retail environment
- Fixing the bank's lackluster customer service, which was damaged by rapid growth

DATA: BUSINESS WEEK

The announcement last August of Coulter's selection as the next CEO suggests the bank intends to confront its shortcomings. In a move that stunned the industry, the 48-year-old corporate and international banking chief was chosen over several better-known rivals. Coulter represents a dramatic change of style and generation, combining a more systematic approach to management with a willingness to listen and a regard for subordinates. "He has the right kind of ego," says former BofA President Thomas A. Cooper.

The measured, cerebral Coulter wowed board members, who were impressed by his intelligence and business acumen. But what tipped the scales in his favor, they say, were his people skills. "We liked his personality," says a director. "He's very sensitive to people." "Dave is terrific," says Salomon Brothers Inc. investment banker Peter H. Peracca. "The only reason he would not succeed is that Balkan politics beat him."

Ironically, the choice of Coulter was itself bound up in internal politics. Chief Financial Officer Lewis W. Coleman, BofA's second-ranking executive, had been the betting favorite in the race to succeed retiring Chairman and CEO Richard M. Rosenberg, who is 65. But for reasons that remain unclear, Rosenberg turned against his No. 2 man, according to company insiders. He and

Coulter wants to improve customer service, which has suffered while BofA has more than doubled its size

ıe rest of BofA's board passed over ıe CFO and turned instead to Coulter, a eputy of Coleman's, as the bank's ader. Insiders say the decision poi-ned relations between Rosenberg, who ill remain as chairman through May, nd Coleman, who has since left the ank.

From his early background, one ould not have predicted that Coulter ould one day be lauded for his people

BIO

DAVID A. COULTER
President and CEO, BankAmerica

BORN
Pittsburgh, 7/31/47

EDUCATION
BS in mathematics, master's in industrial administration, Carnegie Mellon University, 1971

CAREER
Office of Economic Opportunity
helped organize minority-controlled bank, 1971-73

BankAmerica
Financial analyst (1976–80), assistant to the president (1980–82), head of corporate development (1982–85), head of U.S. corporate banking (1990–93), head of corporate and international banking (1993–95), president and CEO (1996-)

PERSONAL
Lives in San Francisco with his wife, Susan; likes squash, tennis, fly-fishing; roots for 49ers and Giants

DATA: BUSINESS WEEK

kills. The Pittsburgh-born Coulter got egrees in math and industrial adminis-ration at Carnegie Mellon University. 'he training gave him a taste for quan-itative analysis and a bent for building nancial models that has stayed with im throughout his career. "I tend to e pretty analytical," he says.

Coulter joined BofA in 1976 as a fi-ancial analyst, but he soon gained a lum job as assistant to then-President 'om Clausen. Later he moved to corpo-ate planning, where he carried out ıuch of the spadework in the purchases f Seattle-based Seafirst Corp. and dis-ount broker Charles Schwab & Co.

Despite these somewhat technical as-ignments, Coulter was developing polit-:al savvy. In 1985, when he was assis-tant to the head of global banking at BofA, he was asked to help in a delicate assignment: taking authority over worldwide consumer operations from the wholesale managers in his division. That would enable the bank to develop a more coherent consumer strategy. Although BofA's consumer and corporate bankers had nothing but scorn for each other, Coulter took on the task and pulled it off. "Dave's attitude was, 'If it's a corporate priority, I'll do anything I can to help you,'" recalls Les Biller, the retail manager who directed the project. After becoming wholesale chief in 1993, Coulter moved BofA away from an emphasis on traditional lending. Instead, he sought to sell customers a range of credit and noncredit services, such as managing corporate flows of cash. He built sophisticated models to measure how much profit BofA extracted from each customer. And he carried out a wrenching reorganization in which responsibility for liaison with customers was taken from BofA's proud cadre of corporate lending officers and assigned to a newly created group of so-called "relationship managers," for whom credit was just one of many products.

If Coulter, as CEO, is to get a grip on BofA, he will have to start by controlling his senior executives. While he calls reports of infighting at BofA "overstated," he does acknowledge the problem. "I don't think we have functioned as well as a team as we could have," Coulter concedes, though he says he plans no immediate changes in his nine-member managing committee.

One of the most debilitating struggles is taking place in an area where Coulter can least afford it—retail banking, where computers, automated tellers, and telephones are revolutionizing the delivery of financial services. Under Rosenberg, retail banking was divided into two separate baronies, each with its own line to the CEO: Vice-Chairman Thomas E. Peterson's product-development division and a 10-state branch network under another vice-chairman, Luke S. Helms. Helms insisted on the separate reporting relationships when he came to headquarters in 1993 after running the bank's Seafirst subsidiary. But BofA insiders say the arrangement hampered cooperation between the product and sales staffs.

In August, Coulter persuaded Rosenberg to end the schism by combining the divisions into a single unit, with Helms reporting to Peterson. Some BofA watchers think the move could prompt Helms to leave, a loss Coulter can ill afford. The charismatic 52-year-old branch chief is a creative marketer who honed his skills at McDonald's Corp.'s Hamburger University. Through a spokesman, Helms says he loves his job and doesn't intend to go. Coulter says he wants both Helms and Peterson, 60, "to be here for the long term."

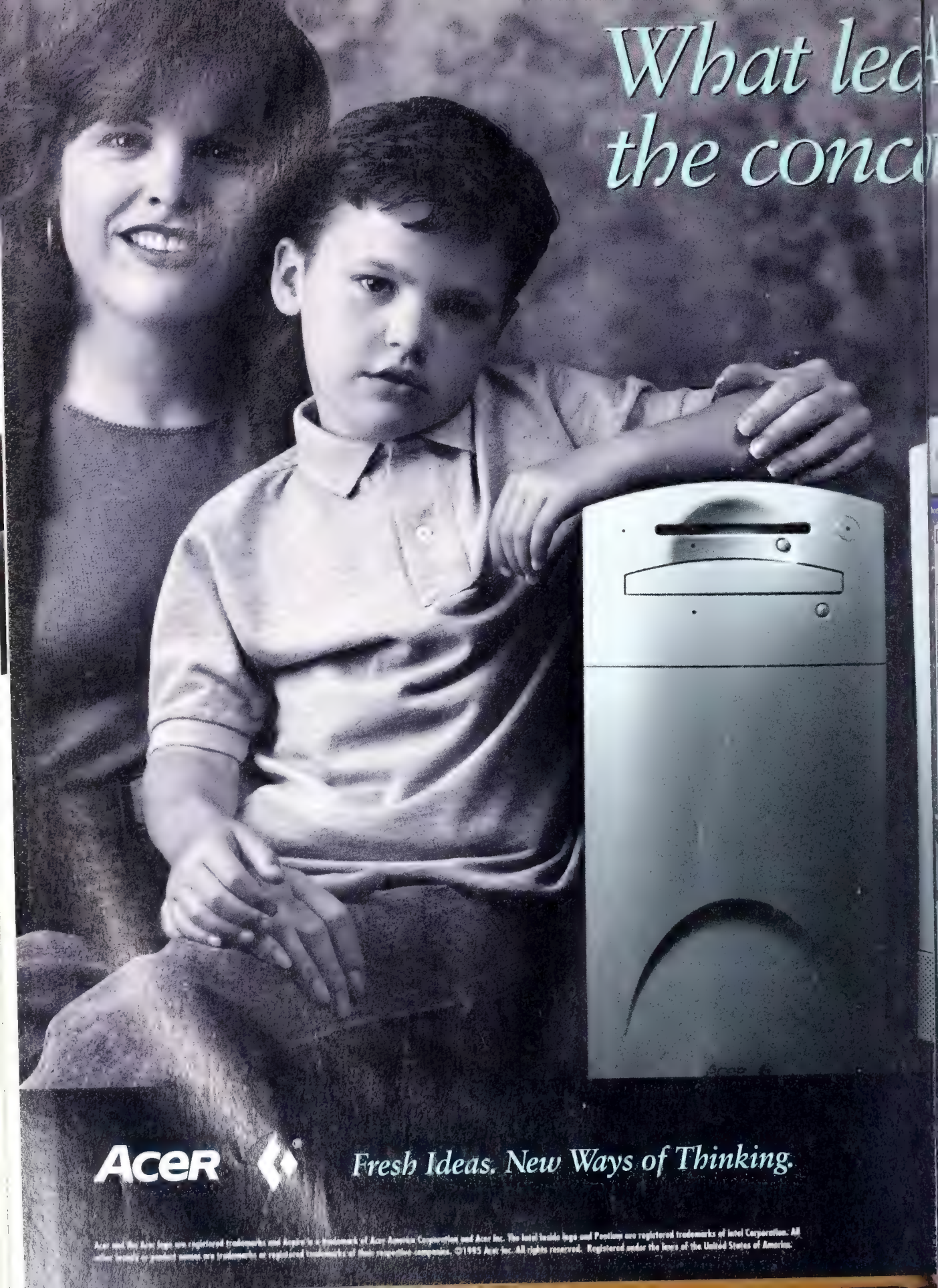
DAY-TO-DAY. On business issues, Coulter says he is focusing on hammering out a formula for BofA's retail businesses as new technologies come on line. A vital part of his retail strategy is making better use of the bank's database, which traces patterns in more than 15 million households that use financial products and services. Says Coulter: "I haven't heard anybody in the industry who can articulate what is exactly the long-term economic model for making money in the consumer finance business."

Coulter is working to improve the bank's laggard level of customer service, too, which has suffered while BofA more than doubled in size over the past five years. Coulter praises the franchise handed to him, but he says rapid growth has taken the bank's eyes off day-to-day delivery of services. "We need to work on execution," he declares.

Growth is not on Coulter's agenda. Rosenberg spent a fair amount of time plotting deals with an array of giant banks, including NationsBank, Chase Manhattan, Bank of Boston, and First Bank System. But Coulter argues that few deals really pay off for shareholders. "It's my job to talk," he says. "But I come to most mergers with a pessimistic bent."

Coulter will have his hands full simply grappling with BofA's intractable bureaucratic inertia. "I don't want to be looked back on as the person who maintained the bureaucracy of BofA," he declares. But that system has worn down more than a few BofA managers. Coulter will need all his talents to avoid becoming one of them.

By Sam Zuckerman in San Francisco



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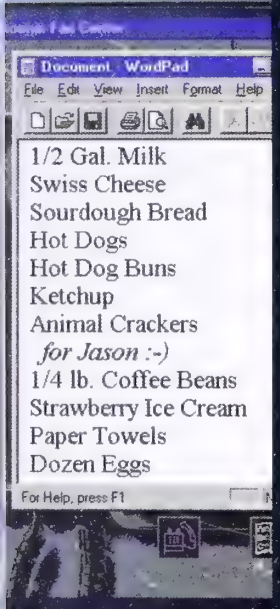

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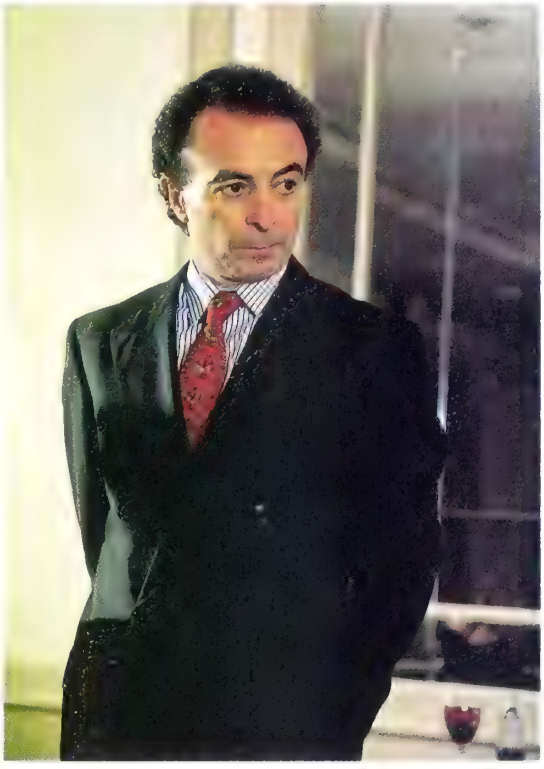
BANKING

TOSSING A LIFELINE TO MEXICO'S BIGGEST BANKS

Even Banamex and Bancomer are getting a state bailout

Mexico's yearlong economic crisis has been murder on the country's banking system. The government has been forced to take over six banks and bail out nine others. But the prevailing wisdom was always that the system's crown jewels, Banamex and Bancomer, would easily weather the storm. Now they, too, are in sufficient distress that the government is preparing to assume chunks of their troubled loan portfolios—and those of two other banks. The cost: more than $4 billion on top of the $11 billion the government has already spent on bailouts. The government effort has grown so massive that some critics are saying that the banks are being gradually renationalized.



ORTIZ: *The bank privatization was mishandled*

It's a stunning reversal. Just four years ago, the government made $13.5 billion selling off the state-controlled banks to some of Mexico's cockiest entrepreneurs. They plunked down an average of three times book value for 18 banks, figuring that the economic reforms of then President Carlos Salinas de Gortari, coupled with free trade with the U.S., would guarantee vigorous economic growth and handsome profits.

SICK SYSTEM. Instead, the new owners have seen the value of their holdings devastated by the high interest rates and bad loans that are the hallmarks of the financial crisis. With borrowers unable to pay, past-due loans now exceed $17 billion—18% of the system's portfolio. If tougher U.S. accounting standards were applied, the figure would be as high as 35%—meaning the system is very sick.

The banks' problems present a big threat to President Ernesto Zedillo Ponce de León's pledges that the economy will recover in 1996. The country needs healthy banks to finance any recovery. Yet, Standard & Poor's Corp. says Mexican banks won't start to turn around until the third quarter of 1996, because banks and borrowers are still being hit by 50% interest rates.

The worry is that Mexico's banking problems will be a drag on the economy for years. Moody's Investors Service warns that the bank bailout could cost 10% to 15% of GDP, or up to $40 billion, over the next 15 years. That would slow growth and suck Mexican and international funding away from other uses. With the economy expected to shrink in early 1996, the government may have to step in with more money soon. "The government is providing Band-Aids to the banks as they come for help, but the real cancer—the past-due loans—has not been eliminated," says economist Rogelio Ramírez de la O.

The government doesn't have any easy way out of this mess. If officials try to help the banks by bringing rates down too quickly, the markets will likely pummel the peso and Mexican securities. That's what happened last fall when market jitters forced an upward spike in rates, producing a flurry of new defaults.

WARY INVESTORS. Despite the banks' woes, their stocks have risen along with the Mexican Bolsa index since October, when investors who believed that growth would return to Mexico in 1996 decided to get in while the market was cheap. But also in October, Standard & Poor's downgraded Banamex' peso debt to BBB–, S&P's lowest investment-grade rating. In response, the loan-buyout program, previously used to help smaller banks, was extended to Banamex and Bancomer, which together control 39% of the system's assets. "Banamex and Bancomer are the most important banks in Mexico, and we simply can't run the risk that their finances might deteriorate," says Eduardo Fernández, president of Mexico's Banking & Securities Commission.

The banks' troubles present a buying opportunity for foreign banks—though most are wary of getting entangled in a Mexican bank now. But Spain's Banco Bilbao Vizcaya paid $340 million to buy control of troubled Mercantíl Probursa in July. Canada's Bank of Nova Scotia is negotiating to assume control of Inverlat. And Bancomer is shopping around for a foreign minority investor to inject fresh capital.

Mexican officials concede that their handling of the bank sell-off in the early 1990s contributed to the sector's current problems. Too much emphasis was placed on obtaining high prices and too little on the buyers' banking skills. "In retrospect, I would have applied some of the purchase price to better capitalization of the banks," says Finance Secretary Guillermo Ortiz, who was in charge of the privatization program then and is responsible for bailing the banks out now. He may have to spend years putting them back on the road to health.

By Geri Smith in Mexico City

HIGH ANXIETY "The government is providing Band-Aids..., but the real cancer–the past-due loans–has not been eliminated"

KEMPER: NOW IT'S ON A SWISS WATCH

The mutual funds' new owners demand a two-year turnaround

For mutual-fund companies overall, the 1990s have been one long celebration. Thanks to strong markets and billions in new cash, the mutual-fund industry has nearly tripled since 1990. But for insurance giant Kemper Corp., the festivities never really began. Over the past five years, Kemper mutual funds have been dead in the water, as management doled out product development and marketing bucks with an eye dropper in pursuit of short-term profits.

Now the Kemper funds are trying to get moving again. New owner Zurich Insurance Group, which took over Kemper Jan. 4, has approved a rebuilding plan that sacrifices near-term earnings to restore marketing, distribution, and talent. Under a new name, Zurich Kemper Investments Inc., the Kemper funds are making their first aggressive push for assets in years (chart).

The goal: beef up the funds from $44 billion in 1995 to $70 billion by 2000. "We've got to get this ship moving again," asserts Stephen B. Timbers, the 51-year-old growth-stock expert who is spearheading this ambitious strategy.

For Kemper, however, the new initiative is unlikely to pay off soon. For one thing, the brokers, bank reps, and financial planners who peddle Kemper's line of load funds will want results before they champion the stagnant franchise again. Despite a recent spate of good performance, Kemper will need time to overcome the bad stretch in its equity-fund track record and fill long-standing gaps in its product line by introducing international stock funds, for instance.

RECRUITING STARS. Yet Kemper has strengths, too: Its fixed-income performance has been robust, its name remains golden with many investors, and its size gives it enviable scale. "If they get their act together, they could be a tough competitor. But you don't get there overnight," notes Jon S. Fossel, chairman of the competing Oppenheimer Funds Inc.

The task of restoring Kemper falls to Timbers, who led the asset management unit to a rare string of successes from 1989 to 1991. Rewarded with the No. 2 job at parent Kemper in 1992, he became embroiled in chaotic buyout talks with General Electric Co. and Conseco Inc. After those bids slipped away and Zurich's prevailed a year ago, Timbers returned last spring to the asset management unit with big plans. He is pumping up the marketing budget from $2 million or so to as much as $20 million this year—an aggressive TV ad campaign breaks in March. He is nearly doubling the sales force and recruiting such star investment talent as Steven H. Reynolds of Alliance Capital Management, who took over Kemper's $12 billion equity department in September.

Timbers' new bosses are giving him roughly two years to show results. Since Kemper funds have been "undermarketed," Zurich will tolerate flat operating profits as the firm rebuilds, says CEO Rolf Hüppi, who spent $2 billion on the acquisition, which includes Kemper insurance holdings. Yet while Timbers gets autonomy and a war chest for now, he must move fast to meet Zurich's ultimate objective: building a global retail operation that sells Kemper funds from Switzerland to Australia. Timbers concedes his job is on the line. If the Kemper funds fail to meet their performance objectives in two or three years, he says, "you'll be talking to somebody new."

Restoring Kemper funds would be easier if its former parent hadn't milked them. For years, Kemper used profits from its mutual-fund operations to compensate for other corporate woes, such as debilitating real estate losses. A revolving door—the equity funds have had three chief investment officers in four years—discouraged top portfolio managers. Morale began sinking when growth-fund star Ronald C. Ognar, now at Strong Funds in Milwaukee, left Kemper in 1991. Small-company stock-picker Beth Cotner, an 11-year Kemper veteran who recently left for Putnam Investments, says: "It's hard for portfolio managers when there's turnover at the top."

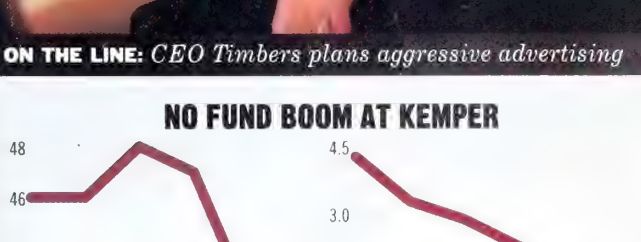
Yet Timbers exudes confidence, and the early results look good. Kemper's performance began rebounding last year, with 93% of its funds in the top half of their peer groups. Sales began turning around in the summer of 1995, as the Zurich deal ended uncertainty about Kemper's immediate future. The spin-off of a securities arm that had competed with other fund distributors has helped, too, Timbers says. And planners and brokers seem to be more receptive recently. "We're trying to do something very bold." That's unusual for Kemper—and long overdue.

By Greg Burns in Chicago

ON THE LINE: *CEO Timbers plans aggressive advertising*

PHOTOGRAPH BY MICHAEL L. ABRAMSON; CHART BY BRIAN HEHMAN/BW

NO FUND BOOM AT KEMPER



DATA: ZURICH KEMPER INVESTMENTS INC., INVESTMENT COMPANY INSTITUTE, BUSINESS WEEK

IT'S A BUY: *Investors queuing up at a Shanghai brokerage firm*

MARKETS

BULLS IN THE CHINA SHOP

Low stock prices and less fear of new markets boost trading

The Chinese New Year doesn't begin until the middle of February, but in one respect, the country already seems to be making a fresh start. Chinese stocks trading in Hong Kong, New York, and Shanghai are staging a surprise rally after plummeting in 1995. The Crédit Lyonnais Securities H-Share Index of Chinese companies listed on the Hong Kong Stock Exchange rose 29%, from 806 on Dec. 27 to 983 on Jan. 5. That's a 44% gain from the record low set on Nov. 16.

Why the sudden interest in Chinese companies? Beijing hasn't announced any dramatic changes in economic policy or market regulation. Instead, many analysts believe, investors are returning to the long-neglected shares almost by default. Mark Mobius, president of Templeton Emerging Markets Fund, cites three reasons for the turnaround. First, the sharp rise in U.S. markets in 1995 is forcing international fund managers to diversify their assets as they search for value. Second, Chinese stocks are cheap, often trading at price-earnings ratios in the single digits. Finally, Mobius believes that the "tequila effect" that dogged all emerging economies after Mexico's peso crisis a year ago is ending. "People are feeling more calm about developing markets," he says.

With liquidity pouring into Asia, trading volume in Chinese stocks is swelling for the first time in months. After hovering between 3 million and 5 million shares a day for more than three months, volume on the Shanghai bourse shot up to 15 million shares a day during the first week of January. Although much of that activity was local, foreign buying and selling was going on, too. "We've seen a lot of [international] fund managers coming up and saying, 'What can we stomach?'" says John Crossman, who heads Jardine Fleming's office in Shanghai. U.S. investors abroad—who prefer Chinese companies' American depositary receipts to H shares, which trade on the Hong Kong exchange, or B shares, which trade in Shanghai—also jumped on the bandwagon, sharply driving up prices of Chinese ADRs (table).

THE CHINA RALLY

COMPANY NAME	ADR PRICE ON 1/10	PERCENT CHANGE SINCE 12/22
BRILLIANCE CHINA AUTOMOTIVE	$6.50	79%
CHINA TIRE	$11.25	104%
EK CHOR CHINA MOTORCYCLE	$14.25	22%
HUANENG POWER	$16.50	13%
SHANGHAI PETROCHEMICAL	$31.50	16%

DATA: BLOOMBERG FINANCIAL MARKETS

Some investors see bigger gains ahead. Virginie Maisonneuve, Southeast Asia portfolio manager for Batterymarch Financial Management Inc. in Boston, has been taking profits from domestic Hong Kong companies, whose shares were up about 30% in 1995, and switching money into H shares and B shares. Besides considering Chinese stocks cheap, Maisonneuve sees a bullish signal: In March, the National People's Congress will ratify the country's next five-year plan, and historically monetary policy has been "more relaxed" in a plan's early years. Maisonneuve believes easier credit will prompt investors to reevaluate Chinese companies. "Sentiment is going to change," she predicts.

PROBLEMS REMAIN. Not all observers are that sanguine. Indeed, while Beijing authorities may have gotten a grip on inflation and engineered an economic soft landing, many worrisome questions still remain. Among them: how to loosen credit controls without rekindling inflationary fires, how to restructure or rescue China's bankrupt state enterprises, and how to shift economic development away from the coast to the hinterland. The fate of financial-market reforms as well as the post-Deng political succession also remain up in the air. "There has been no change in the fundamentals for Chinese companies," insists Goldman Sachs & Co. Hong Kong analyst Janice Wallace.

Yet the cheapness of their stocks seems to have won some converts. Price-earnings ratios as low as 5 or 6 induced Peter Churchouse, head of research at Morgan Stanley Asia Ltd. in Hong Kong, to jump into the Chinese market in early December. Churchouse loaded up on the Hong Kong-listed shares of Zhenhai Refining, Yizheng Chemical, and Qingling Motors. All obligingly rose.

Whether the rally has long-term momentum is still a guess. Chinese economic and regulatory policy tends to move in lurches, and its corporate managers have enraged foreign shareholders on more than one occasion. Yet the new year has emboldened investors. "Look, these aren't the best companies in the world," says Mobius, "and the people who run them aren't open. But the bottom line is that China continues to grow." That bottom line—plus rock-bottom prices—could be what gives Chinese stocks more room to rise.

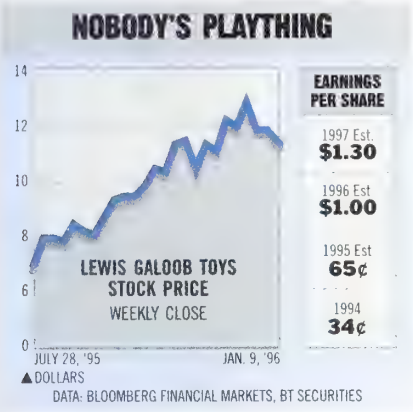
By Dave Lindorff in Hong Kong, with William Glasgall in New York

BY GENE G. MARCIAL

A KNOCK AT THE TOY SHOP DOOR?

It has been a while since toymakers have caught investors' fancy—with the Street so bored with the industry. But is there another Mattel or Hasbro likely to become a winner? Some pros think so: They're betting on Lewis Galoob Toys (GAL), particularly after the notice some of its products got during the Christmas rush.

"The key in the toy business is longevity," says Gary Jacobson, toy industry analyst at BT Securities, a Bankers Trust unit. He explains that Galoob lines such as Micro Machines and My Pretty Dollhouse have become staples—unlike some rivals' toys, which can be faddish.



And precisely because other makers think such toys give Galoob staying power, the company is perceived as takeover bait. One money manager says: "I am sure Mattel and Hasbro have been considering a move on Galoob, especially after the brisk sales of its new Sky Dancers line during the holidays." Sky Dancers are ballerina dolls that spin and flutter into the air when lofted from a handheld launcher.

In a buyout, Galoob shares, now trading on the Big Board at around 11, would be worth 20 to 25, reckons the money manager. One big buyer of the stock is Fidelity Management, which had upped its stake from 8.5% to 9.9% as of the end of September.

Jacobson says he doesn't know if Mattel or Hasbro has approached Galoob, but he, too, believes the company would be "an excellent" acquisition for either. "Galoob has proved it can turn out products with long-lasting appeal, and that's exactly what Mattel and Hasbro are looking for," he says. "As long as Galoob continues to have product momentum, it will either grow or be acquired," says Jacobson. At February's Toy Fair, Galoob will introduce new lines that he says will include Dragon Fliers—airborne figures designed for boys.

He says that the industry has been consolidating and that fierce competition will make for more mergers and acquisitions this year.

Analyst Phillip Seligman of Value Line notes there is pressure on toymakers from multimedia personal computers and CD-ROM software, which offer features that compete with traditional toys. He thinks the answer is diversity—which Mattel, Hasbro, and Tyco Toys have been pursuing.

Even with no takeover, Jacobson says Galoob is undervalued. Extra push will come from Galoob's exclusive pact with Twentieth Century Fox, signed in October, to license toys based on Fox film and TV properties. Mattel says it's always on the lookout for acquisitions. Hasbro and Galoob didn't respond.

THE STRONG PULSE AT RAYTEL

Although the initial public offering market has been a scorcher, not every IPO got swept up. A case in point: Raytel Medical (RTEL), whose shares went public in early December at 8. The stock hasn't seen much action—and is currently at 9.

But that seems just dandy to the investment chief of a large mutual fund who is scouting for promising young companies in the health-care business—particularly those focusing on cardiovascular disease. Raytel is a major provider of specialized "transtelephonic" pacemakers and a leader in detection of "cardiac events." This fund manager thinks the stock is worth twice its current price, based on growing demand for such services.

Pacemaker monitoring is used by cardiologists and internists to evaluate periodically the "interaction of implanted pacemakers with a patient's heart," explains John Girton, an analyst at Van Kasper, which is a co-underwriter of the IPO. "Cardiac-event detection," he adds, is prescribed by cardiologists to capture "transient irregular heart rhythms" of patients with certain types of cardiovascular disease.

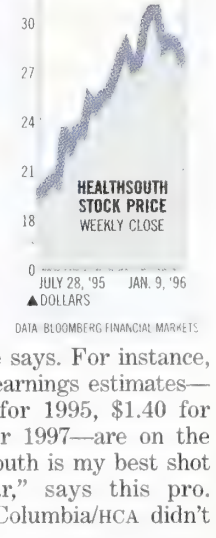
The analyst thinks earnings for the year ending Sept. 30 will jump 26%, to 95¢ a share and revenues will climb 25%, to $89.4 million. With Internet stocks on the wane, this manager is betting that the next market stars will be in health care and medical services.

HEALTHSOUTH MAY GET THE TREATMENT

Healthsouth (HRC), the nation's largest provider of outpatient and rehab health-care services, has been on an acquisition binge, accumulating 500 treatment centers in 38 states. But now, Healthsouth itself may be a target.

According to several investment bankers, Healthsouth has caught the eye of a logical suitor: Columbia/HCA Healthcare, the largest U.S. hospital-management company, which has grown by means of an aggressive M&A program. Healthsouth's growth should reflect the current strong demand for rehab treatment, says one money manager. He notes that Healthsouth's facilities feed on pressure from insurers to move patients out of regular hospitals to the less costly rehab centers.

Columbia/HCA owns and operates some 285 acute-care and 28 psychiatric hospitals in 36 states—and in Britain and Switzerland. It also owns more than 125 outpatient centers. "So the strategic and geographic fit is all there between Columbia/HCA and Healthsouth," says one investment manager, who owns nearly 5% of the stock. He calculates that, in a takeover, Healthsouth shares, now at 27, would be worth 45. On Jan. 10 the stock jumped to 29, partly because of another analyst's "strong buy" recommendation.



This investment pro says the stock is undervalued—based on earnings growth alone. "The Street is underestimating Healthsouth's earning power," he says. For instance, he thinks current earnings estimates—of $1.10 a share for 1995, $1.40 for 1996, and $1.80 for 1997—are on the low side. "Healthsouth is my best shot for the new year," says this pro. Healthsouth and Columbia/HCA didn't return calls.

CONSULTANTS

NEVER MIND THE BUZZWORDS. ROLL UP YOUR SLEEVES

The Feigenbaum brothers' advice is pragmatic, and it saves companies big bucks

Only a few weeks earlier, Armand "Val" Feigenbaum had been in the hospital for a double hip replacement. The last thing Tenneco Chairman Dana G. Mead expected was to see the 75-year-old quality guru stroll into corporate headquarters in Houston, 1,800 miles from Feigenbaum's home, for a routine meeting. "Before you know it, Val was challenging me to a tennis match," laughs Mead.

But that's the kind of work ethic people have come to expect from Val and his kid brother, Donald S., 70. For nearly three decades, these former General Electric Co. engineers, working behind the scenes, have been streamlining operations at many top corporations. As principals of General Systems Co. in Pittsfield, Mass., with revenues of $20 million a year, the brothers have assembled an enviable list of clients, including Tenneco, Union Pacific, Citicorp, Pirelli, 3M, and Johnson Controls.

Although less well-known than the late W. Edward Deming or Joseph M. Juran, Val Feigenbaum, too, is one of the founding fathers of quality. While Deming emerged as the movement's visionary and Juran became its teacher and trainer, Feigenbaum, who wrote *Total Quality Control* 45 years ago, is the hands-on implementer.

"STEALTH GURU." He and Don shun the consultant tag. They consider themselves engineers who focus on the nitty-gritty details of what makes business work. "Management isn't an art to them. It's a science," says James L. Bailey, an executive vice-president at Citicorp, which hired the brothers to improve credit-card operations. "They break business down into discrete pieces and examine it."

The goal is to drive out of operations "failure costs"—the aggregate cost of failing to do things right. Eliminating one inefficiency—a defect, say, or an excessively complex process—reduces total product costs, Val notes. "Less money is spent on inspection, complaints, and product service, for instance," he says. Moreover, as you reduce failure costs, "by definition you improve customer satisfaction." The Feigenbaums estimate that failure costs average 25% of gross sales in most major American companies. At world-class companies, however, they are no greater than 10%.

Failure costs at Tenneco Inc. were running at 22%, or $2.9 billion, in 1991, when the late Michael H. Walsh, then chairman, called in the Feigenbaums and a team of their engineers. In one division, they discovered that the company was wasting 20% to 40% of the material being machined for auto parts. Merely changing the way the raw goods were fed into machines eliminated the waste.

Since 1991, Tenneco has cut a total of $1.8 billion in failure costs, which resulted in an extra $900 million in operating income. Such a return, Mead says, makes paying the Feigenbaums' fee—nearly $20 million for five years' work—"a no-brainer." Adds another client: "I don't think they charge what they're worth. Obviously, they aren't worried about where the next meal is coming from. They're more interested in making a contribution."

Both brothers fit the stereotype of New Englanders as reserved, hard-working, pragmatic, and conservative. Tenneco's Mead dubs Val his "stealth guru" because of his unassuming personality. The duo shun buzzwords and acronyms, and they disdain slash-and-burn cost reduction, management fads, and quick fixes. Their approach calls for a roll-up-your-sleeves analysis of each step in a business process. "We've always been skeptics about selling labels," says Val. "We're about creating results and relationships with customers."

For two men who have the ear of some of the most powerful executives in the U.S. and Europe, Val and Don share a remarkably untouched quality. Their modest center-hall Colonial house in Pittsfield is just a half-mile from where they grew up.

Never married, the two live, work, socialize, and relax together. A treasured possession is the still-evolving Lionel train layout in their basement. Both

Squeezing Out Inefficien

CLIENT	RESULT
UNION PACIFIC	Upgrading the railroad's scheduling, maint nance, and customer service has eliminat more than $700 million a year in "failure costs" since 1988
TENNECO	Company teams, with Feigenbaum help, improved operations, yielding $250 millio a year in extra operating income
CITICORP	A two-year assignment significantly impro customer retention by the bank's credit-ca operation
DEERE	Tractors and other agricultural implement are now designed, produced, and sold using systems that were created by the Feigenbaums
CUMMINS ENGINE	The company has, with advice from the Feigenbaums, beaten back a challenge by Japan's Komatsu

DATA: BUSINESS WEEK

The objective is to drive out "failure costs"—the tot

lay the piano: Don favors Beethoven nd Brahms, while Val enjoys Chopin. Val's hip replacements let the brothers continue a good-natured sports rivalry: On the links, Val usually bests Don, who often gets his revenge at tennis. Other than the normal kinds of fights hat any two people have, we've always gotten along very well," says Don. "We ave a complementary relationship."

TOOLMAKER. Another thing the brothers hare is devotion to their late mother, Hilda Vallin, a concert pianist who instilled in them a fascination with education and the arts. Their house seems a ear-shrine to her. The eulogy that Val elivered at her funeral in 1963 sits vith her framed photo atop the grand iano. It is bound in black leather and ears the title "A Beautiful Person." Her dishes are displayed in the dining oom cabinet. In her honor, the brothers ave endowed a room in the Berkshire Athenaeum and sponsor an annual lecure at a local temple.

However, it was their father, Samuel Frederick Feigenbaum, a CPA who ran his own accounting firm, who advised Val to skip college and go straight from Pittsfield High School to work for GE as an apprentice toolmaker in 1937. "His point was that if I wanted to be an engineer, I should learn how to make things with my hands," recalls Val. "It always gave me an edge."

While on GE's payroll, Val earned a trio of degrees, including a doctorate in economics from Massachusetts Institute of Technology. He climbed the corporate ladder quickly, becoming director of quality at GE's expansive Schenectady (N. Y.) operations at 23.

In 1946, after a stint in the Navy, Don also joined GE as an engineer. Eventually he became a manager in the company's jet engine business. In 1961, he left GE to become general manager of consultants International Systems Co. He was already something of a pioneer in "value engineering"—a method of exploring whether parts or products can be made in a cheaper and more cost-effective way. In 1968, Val—by then GE's worldwide director of manufacturing and quality control—gave up his 34th-floor office on New York's Park Avenue to join Don in launching General Systems from their hometown in the Berkshires.

Between them, the brothers had 42 years of GE operating experience—and a Rolodex full of contacts. Their very first morning in business, they received a call from Volvo of Sweden that led to their first assignment, a two-year job applying systems-engineering techniques. Success there led to work for Fiat, Pirelli, Renault, Alfa Romeo, and Volkswagen. In the U. S., two companies run by former GE executives, Memorex and compressor maker Copeland Corp., were their first clients. General Systems now employs about 110 people.

In every assignment, the pair work closely with client teams, guiding them through an engineering methodology—their "technology"—that scrutinizes each part of a business process. "The first step is to define what the costs of failure are and to measure them very clearly," says Val. "What you are doing is putting in the hands of people a way to manage the improvement in value and costs." At Tenneco's shipyard operations, he says, failure costs were regularly posted on boards to keep employees abreast of their progress in getting rid of them.

"WISE OLD FOX." To gain the support and enthusiasm of employees, the Feigenbaums aim for quick results. "Results become self-generating," says Don. "When people see it's going to help, it jacks them up to go to the next level." Says Tenneco's Mead: "Half of these quality programs that get grafted onto companies wither and die because they don't have the buy-in and participation of the employees. Val and Don lead our people through the work, but they let us come up with the answers. It gets our people deeply involved in the process."

ENGINEERS AT HOME
Don (rear) and Val Feigenbaum "break business down into discrete pieces and examine it," says a satisfied client

While General Systems' business picked up at the height of the quality movement in the late 1980s, it by no means boomed. Neither has it waned since quality passed its peak as a management trend. "A good deal of the [quality] explosion was for training and speech-making," says Val. "The solid core of what we do—implementation—grew more gradually and hasn't stopped growing."

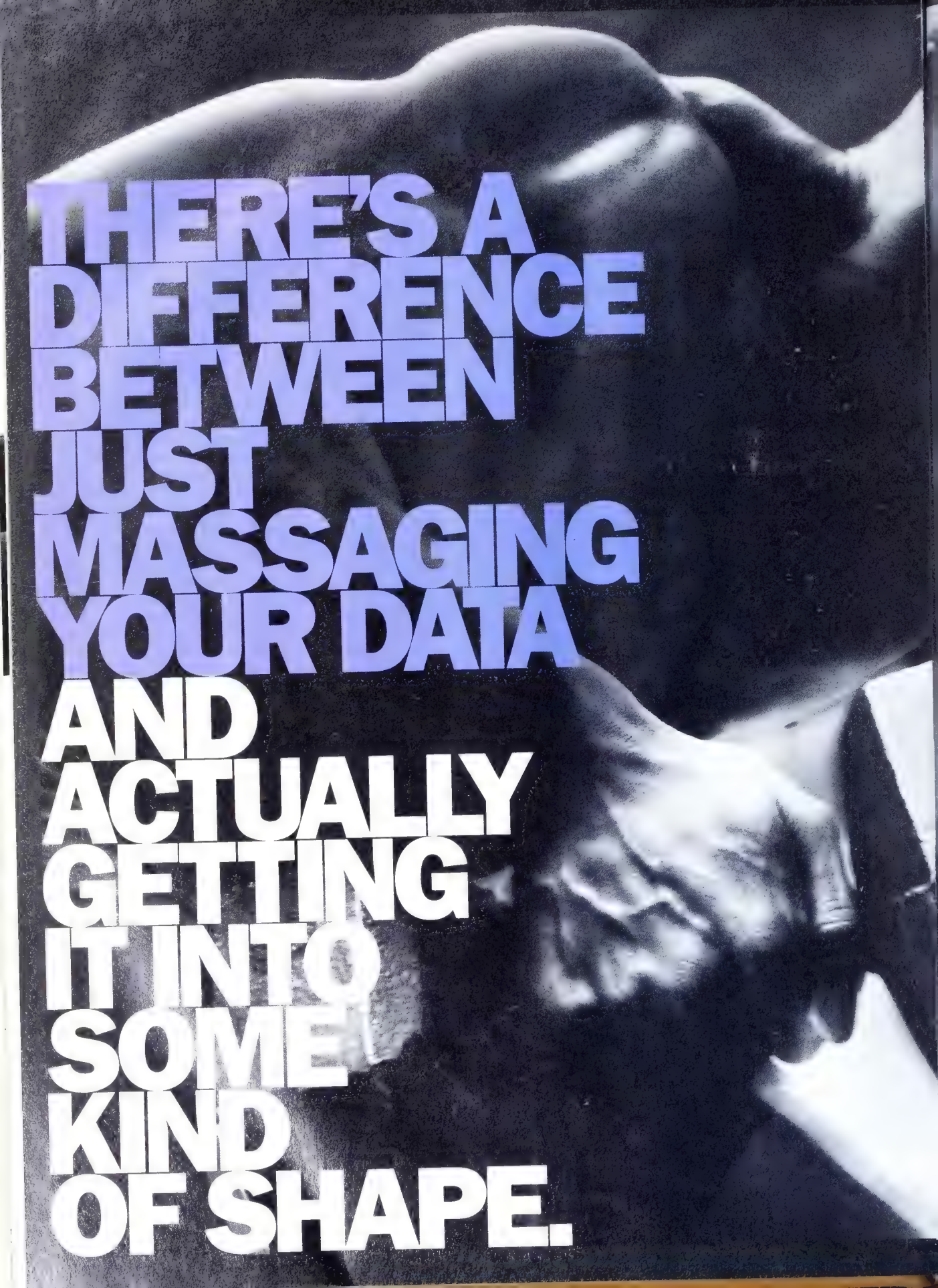
Part of what clients are paying for, of course, is experience. The Feigenbaums have seen the same inefficiencies at companies around the world. "Val's a wise old fox," says Richard K. Davidson, chairman of client Union Pacific Railroad, who credits the Feigenbaums with cutting derailment costs by more than 50%, from $84 million to $38 million. "He has climbed the mountain to look at the bear many times."

Small wonder the brothers see no reason even to think of retirement. "My grandmother had an expression that people rust out a lot faster than they wear out," says Don. "We wouldn't be happy unless we were active. We're doing what interests us. It's fun, and it's rewarding to see results."

By John A. Byrne in Pittsfield, Mass.

pense of not running business operations the right way

DOUG JEVERE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TURNAROUNDS

PACESETTING: *R&D spending is up to $230 million*

ONE COMPANY, TWO CULTURES

How Bill George made it work at Medtronic

Back in 1991, when William W. George swept into the corner office at Medtronic Inc. reciting Tennyson, waxing philosophic about corporate "reinvention," and vowing to triple sales within five years, he drew incredulous stares. Some viewed the Harvard MBA as overzealous; others feared his big-company past at Honeywell Inc. might clash with the risk-taking culture that had made the $1 billion Medtronic the world's leading supplier of heart pacemakers. "We had good momentum," says one veteran exec. "We didn't want to lose it."

But for years, Medtronic's sometimes reckless pace had been the source of its problems. Ever since Minneapolis-based Medtronic invented the pacemaker in 1957, it had flourished technologically by attracting top-notch scientists and giving them free rein. But through much of the 1980s, earnings growth slowed and market share fell as Medtronic spent the better part of a decade fighting a bloated cost structure and the effects of poor diversification.

Now, George—a 53-year-old engineer who capped 11 years at Honeywell as head of its space and aviation systems business—has created momentum of a different sort. He was hired to bring some big-company discipline to Medtronic, and the company today is both technologically strong and financially healthy. "George has come up smelling like a rose," says Kurt Kruger, an analyst with Hambrecht & Quist Inc.

BIGGEST GAINS. George certainly has investors' hearts racing: Since 1991, earnings have risen 120%, to nearly $300 million, while sales are up 70%, to $1.7 billion. For the year that will end in April, Piper Jaffray Inc. analyst Arch C. Smith expects income to rise 29%, to $381 million, on sales of $2.1 billion. Medtronic's stock shot from 20 in mid-1994 to a high of 60 in December, though fears that rivals are cutting into its lead have since sent it below 50.

George began by imposing a tougher regime on Medtronic's designers and its manufacturing division. "This company needed to have two different cultures operating in the same company," says George. "One highly disciplined culture, and the other free-spirited and experimental."

GEORGE: *His efforts halved product-development time*

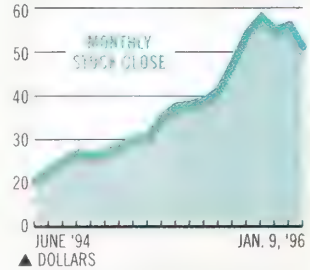
The biggest gains came from pushing the two sides into teams, enabling Medtronic to trim manufacturing inefficiencies even as its researchers paid more attention to the market's needs.

In the past, for example, Medtronic designed new computer chips for every new pacemaker model it developed. George has since scrapped that process. Instead, he had Medtronic develop one microprocessor chip that can be used in different models. The switch cut development cycles by 50%—and since March, 1994, when Medtronic rolled out six new pacemakers at once using the chip, sales are up 15% in a market up 4%.

At the same time, George has poured money into research—R&D spending is $230 million this year, roughly 11% of sales. By setting up a five-member review team that sets strict timetables and financial criteria for projects, the company now gets more bang for its buck. And George is broadening Medtronic's applications: One scientist at its Dutch research center wants to treat stomach disorders with pacemaker technology. "We don't know what they'll bring back," George says. "But if we get something, we know it'll be big."

Today, Medtronic again dominates the market for cardiovascular therapy devices. With a 45% share in the $5.5 billion industry, it's more than double the size of Minneapolis-based Guidant/CPI. But rivals are challenging its lead. Medical products maker St. Jude Medical Inc. just inked a deal with hospital giant Columbia/HCA-Healthcare Corp. to be a preferred vendor of cardiac products. "This deal allows us to be much more competitive with Medtronic," says E. Phillip Palmer, vice-president of corporate development. More worrying, in recent weeks both Guidant/CPI and No. 3 Ventritex Inc. have won FDA approval for new products aimed at Medtronic's 50% of the $650 million market for implantable defibrillators, which are used to control runaway heartbeats.

MEDTRONIC ON THE MEND



DATA BLOOMBERG FINANCIAL MARKETS

Wall Street, fearful that Guidant's tiny new device will allow it to leapfrog Medtronic in the fast-growing, high-margin segment, sent Medtronic's shares tumbling on the news. Although Medtronic has a new defibrillator coming out soon to match Guidant's, analysts say that its once clear lead will give way to a much more even race. With other new products expected soon—including a new family of pacemakers in 1996 and, eventually, technologies for diseases such as Alzheimer's and Parkinson's—Medtronic still has plenty of momentum on its side. But the battle is heating up.

By Ron Stodghill II in Minneapolis

COMPENSATION

A MODEL INCENTIVE PLAN GETS CAUGHT IN A VISE

Lincoln Electric's remake forces a shift toward traditional pay

In recent years, Corporate America has rushed to embrace the idea of motivating employees by linking pay to performance. Nearly half of large companies have tilted their pay systems in this direction, surveys show, and many say they're eager to push the notion further. To learn more, thousands of managers flock to Cleveland-based Lincoln Electric Co. each year to look at one of the country's oldest and most radical pay-for-performance systems.

Unfortunately, the Lincoln model isn't quite the smashing success it once was. After management stumbles forced the family-controlled manufacturer of welding equipment and supplies to sell more shares to the public last year, Lincoln increasingly resembles a typical public company. With institutional shareholders and new, independent board members in place, worker bonuses are getting more of a gimlet eye. At the same time, management is readying itself for an expansion drive to remain globally competitive, putting more pressure on the balance sheet. All that has crimped bonuses, even though Lincoln is posting record sales and earnings. For workers who expect high bonuses if they deliver in output, the shift has hurt morale.

So Lincoln is taking its one-of-a-kind pay system in for an overhaul. The company is by no means ready to ditch the incentive plan, which once paid employees up to 100% of their wages in annual performance-linked bonuses. But executives are now considering ways to move toward a more traditional pay scheme and away from the flat percentage-bonus formula. "The bonus is a good program, and it has worked well, but it's got to be modified some," says Director David C. Lincoln, whose father John C. Lincoln founded the company in 1895. Adds Edward E. Lawler, who heads the University of Southern California's Center for Effective Organizations: "One of the issues with Lincoln is how [its pay plan] can survive rapid growth and globalization."

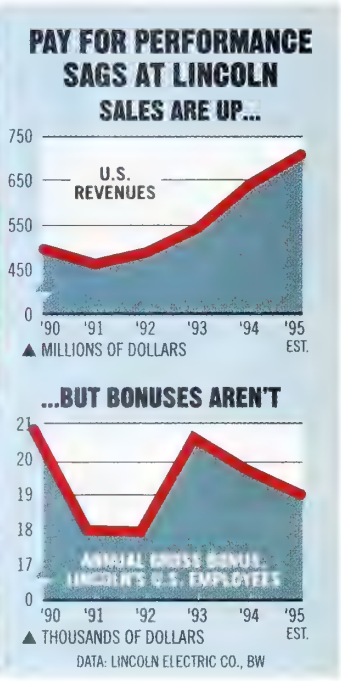
Plans such as Lincoln's may be getting a lot of attention these days, but they date back to the 19th-century piecework system. Each of Lincoln's 3,400 U.S. employees is supposed to be a self-managing entrepreneur. There's minimal supervision. They get paid when they work—no sick or holiday pay. "How much money you make is in your own hands," says Thomas Gadomski, a painting-crew leader.

Each employee is accountable for the quality of his or her own work and is rated twice a year on quality, output, dependability, cooperation, and ideas. The ratings determine how much of the total corporate bonus pool each worker will get, which comes on top of his or her hourly wage.

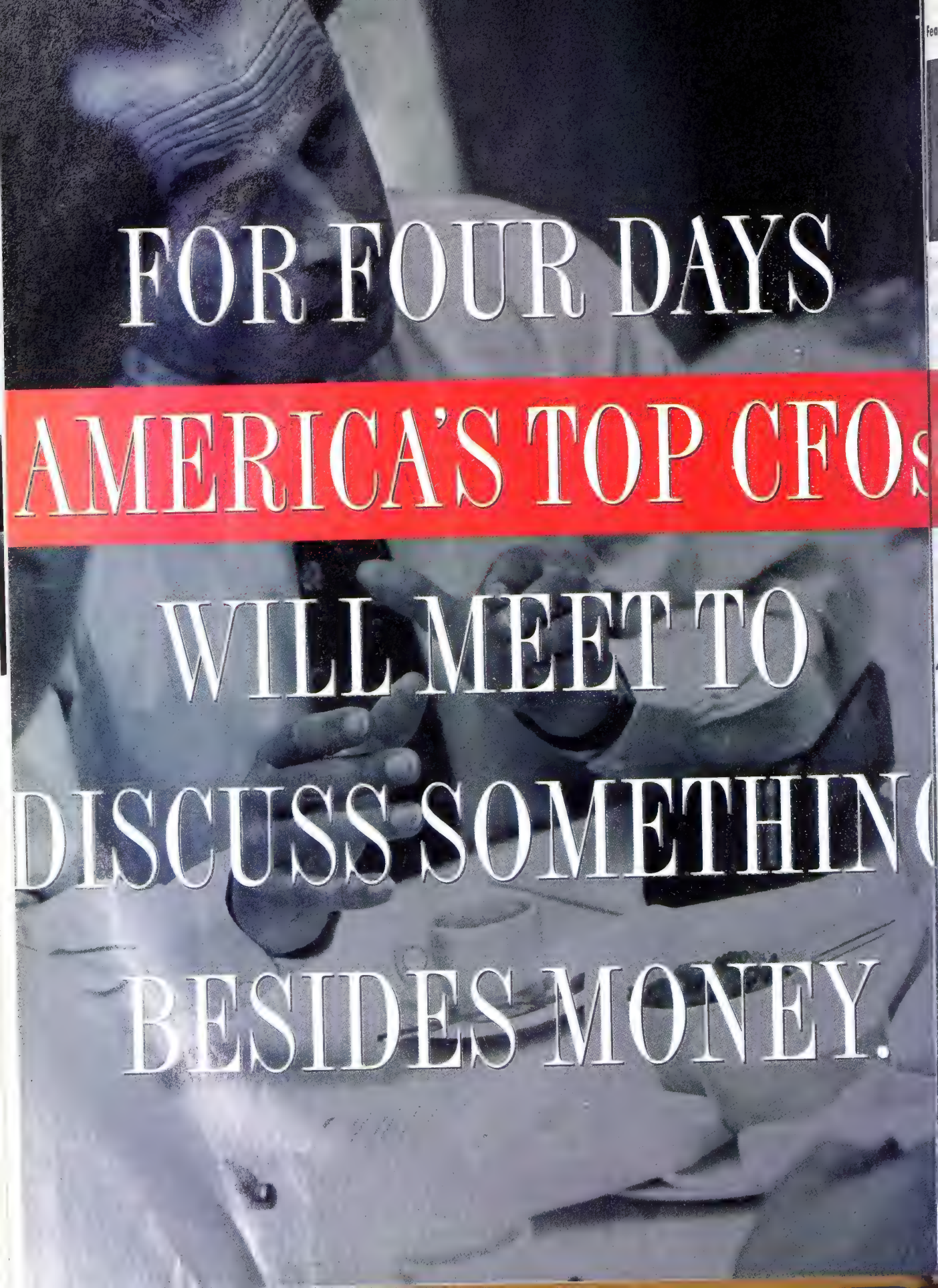
WIDE RANGE. The average Lincoln factory hand earns $16.54 an hour, vs. the $14.25 average manufacturing wage in the Cleveland area. With a 56% average bonus in 1995—the lowest in years—production employees came out ahead of workers elsewhere even after paying for health-care benefits employers typically pick up. But unlike at other companies, Lincoln has huge variations in production-worker pay: from roughly $32,000 to more than $100,000 for the most hard-driving.

There's tremendous pressure to produce, but an employee advisory board meets regularly with top management to air workers' concerns. And Lincoln guarantees work to employees with three years' experience. No one has been laid off since 1948, and turnover is less than 4% among those with at least 180 days on the job. "There isn't any other place to work like Lincoln Electric," says Kathleen Hoenigman, an 18-year veteran. "They take care of you." Indeed, Lincoln went so far as to bor-

GADOMSKI: *Under the longtime system, "how much you make is in your own hands"*



PHOTOGRAPH BY DANIEL LEVIN. CHART BY ERIC HOFFMANN BW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row more than $100 million in 1992 and 1993 to pay U.S. bonuses, even though it lost a total of $84 million in those years, in part because of an ill-conceived foreign-acquisition spree. Says CEO Donald F. Hastings: "I had to go to the board and say: 'We can't break our trust with this group because of management mistakes and recession elsewhere.'"

Still, it gets harder and harder to live up to the old deal. Even though the company has come roaring back after stumbling abroad, the red ink it spewed left Lincoln financially weakened. To make better acquisitions and expand further, Lincoln made its first public offering last July, pushing outsiders' stake to 40%. It also slashed total debt by nearly 40%, to $130 million, and paid a lower bonus per person, though the total bonus kitty was a record $64 million.

PROTESTS. The slimmer bonuses represent a sea change for employees. It didn't help that last year, Lincoln's centennial, was its first with $1 billion in sales. In November, some employees protested outside headquarters after they learned of the bonus size. "Everyone was upset," says one worker. Blue-collar workers had already been disgruntled with management when it set up a lower wage scale in 1993, at 75% of pay, for 700 new employees hired to meet demand and staff an expanded motor operation. Turnover among the new hires was high, and the disparate pay disturbed veterans. "If an individual shows he can handle the workload, he should be rewarded" with full pay, says Joseph Tuck, an inspector with 18 years at Lincoln. Because of the protests, Hastings eliminated the two-tier wage on Dec. 1.

To revamp the pay scheme without stirring up resentment, the company has set up a committee to study the bonus program. It has told employees that a new formula is in the works, and it has hired Price Waterhouse to study productivity. Although Hastings pledges that the incentive system will remain, over time, he wants employees to focus more on their overall earnings, not just the percentage bonus they receive. Already, he has started raising base pay—with a likely reduction of bonuses later—for engineering, sales, and other office staff.

Even after the charges, Lincoln's pay system is likely to remain more innovative than most. But as it tries to hire more outsiders, expand further abroad, and modernize, "we're getting to be a more normal company," says Director Frank L. Steingass. That may not be quite what eager visitors expect to hear. But if Lincoln can adapt to new times without sacrificing employee good will, another model pay plan may yet emerge.

By Zachary Schiller in Cleveland

SEMICONDUCTORS

CAN RUSSIA MAKE UP FOR LOST TIME?

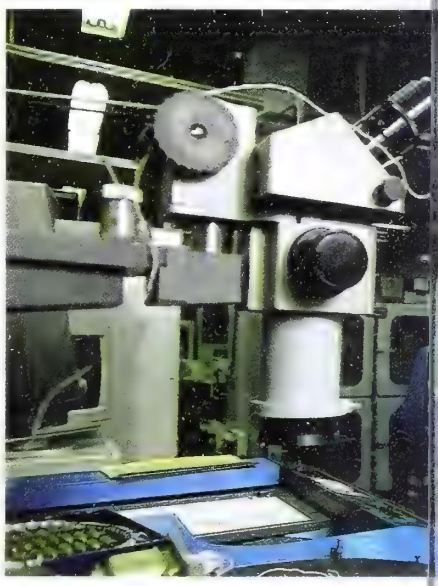
With foreign help, its chip industry tries to regain strength

From the rubble left by the collapse of Communism, Russia's scientific elite once dreamed of building a semiconductor partnership with the U.S. Given access to long-banned Western tools and knowhow, the optimists envisioned Russia's capitalizing on generations of Kremlin-groomed research to become the next South Korea. Instead, years of travail—starting even before the Soviet Union's breakup—reduced the Russian industry to a shadow of its former self.

Finally, there are glimmers of a recovery. Last year, Russia's total chip output increased 10%, to $385 million, ending five years of decline—and sales should grow 7% more in 1996 (chart), predicts British consultant Future Horizons. Chip exports are also taking off—from a paltry $316,000 in 1993 to $19.4 million for the first 10 months of 1995, according to Moscow's official tally. "The industry has definitely turned around," says Future Horizons Chairman Malcolm G. Penn, who specializes in high technology in Eastern Europe.

There are other fresh signs of life: A few top chip companies are opening research operations in Russia, and foreign capital is starting to trickle in. New York investment banker A. Robert Towbin has no doubts that Russia's chip industry will stage an eventual comeback. "It'll just take a few years," says the former chief executive of the Russian-American Enterprise Fund, created by Washington in 1993. Currently, Towbin is raising $50 million for the Grant Unterberg Towbin Russia Fund, sponsored by Unterberg Harris Capital Management and Financial Center Grant, a big Moscow brokerage.

Making up for a decade of neglect will be costly. Some 130 chip factories—90% of

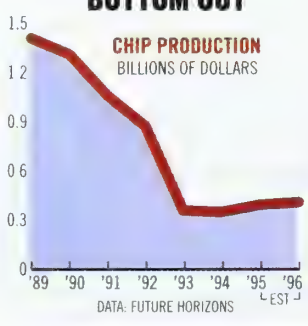


all producers in the old Soviet empire—have closed. The trouble started in the late 1980s, when government grants for capital investment began drying up. And since 1991, defense contracts have withered while runaway inflation has pushed manufacturing costs skyward by as much as 4,000%, reports Mikron Corp., one of only about a dozen surviving Russian chipmakers.

FADED GLORY. As a result, Russia is in the semiconductor caboose. The slimmest lines most companies can print on silicon are a fat 3 microns, or three-thousandths of a millimeter. Such widths date back to the early 1980s and IBM PC/XT computers. Today's mainstream chipmakers are shrinking lines to less than 1 micron, with cutting-edge companies going to 0.3 microns.

Mikron knows it is living on borrowed time, says Yevgeny S. Gornev, deputy director for research and development. Founded

RUSSIAN CHIPS BOTTOM OUT



31 years ago as one of the star residents of Zelenograd, the once top-secret city just north of Moscow, Mikron used to run neck-and-neck with the West. Its Institute of Molecular Electronics was famous for basic research in such areas as superfast gallium arsenide circuits. "In 1985," Gornev boasts, "we had a 1.5-micron clean room"—meaning Mikron could produce then state-of-the-art chips. Ten years later, he concedes, that clean room is still Mikron's best.

To sell its dated chips, Mikron has cultivated low-tech customers in China and Southeast Asia. It claims 20% of the world market for the chips in digital watches, for example. But such chips don't earn enough profits to pay for new chipmaking tools and R&D. Mikron pegs 1995 revenues from 250 million chips at only $20 million. It has halted virtually all basic research.

MIKRON PLANT: *State of the art—for 1985*

The company is pinning its immediate future on joint ventures—starting with a new 1-micron line funded partly by an $18 million equity investment from Hua Ko Electronics Co. in Hong Kong. By February, the plant will begin turning out more upscale chips, including companion chips for microprocessors. Because it uses Eastern European equipment that costs less than Western gear, the plant's total tab was $30 million—a quarter of the price elsewhere. So Hua Ko got a 50% stake in a relatively modern facility for a song.

Such bargains may be Russia's ticket to the big leagues. With chip plants now running at half capacity, Russia could lend a hand to companies struggling to keep up with demand. LG Semicon, the chip arm of Korea's LG Group, recently agreed to supply expertise and equipment to Integral Co. in Minsk, Belarus, so Integral can take over the production of some older LG chips.

REM Capital Corp. of Arlington, Va., sees a similar opportunity in silicon wafers, the disks that chips are printed on. A shortage of wafers will develop this year and become severe by 1999, predicts market researcher Dataquest Inc. So REM Capital is working with Russia's Atomic Energy Ministry to produce ultrapure silicon and wafers in plants that previously refined plutonium. "They could take a good chunk of the silicon-wafer market in five years," says Thomas E. Ward, REM Capital's chief scientist. To fund the project, the company hopes to raise $200 million.

Foreign capital is crucial because hard currency is scarce in Russia, and agriculture and heavy industry have been getting first dibs. Moscow threw some crumbs to high tech last January, launching a special Fund for Electronics Development. But it has only $100 million to spread among chip, computer, and communications companies. Mikron's slice of the pie was just $3.1 million.

SHY SUITORS. Even if capital were plentiful, it wouldn't be enough to put the Russian semiconductor industry back on track. Russia needs technology transfers by the trainload, says Ward of REM Capital. And there's the rub. Two dozen chipmakers have sniffed around Russia, and matchmaking tours have been sponsored by Semiconductor Equipment & Materials International, a trade group of equipment suppliers. But most joint ventures are "still in the tire-kicking stage," says Penn. Primarily, that's due to continuing political uncertainties.

A few Western pioneers are gingerly easing into Russia to tap its scientific talent. Motorola Inc. and Samsung Electronics Co. have set up small R&D centers, and Texas Instruments Inc. might be next. "The Russians have been conducting research more or less in isolation for 50 years, and that has led them to do some unique things," says David R. Thomas, TI's head of R&D in Europe. He sent scouts to Russia last fall, and they came back with valuable ideas in semiconductor materials science and computer software.

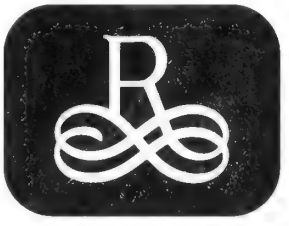
Still, R&D outposts won't do much for Russia's chip industry. It needs help in leapfrogging several generations of production savvy. That could happen in time for the new century if the West pitches in. Otherwise, catching up may take a decade or more. But at least the deterioration of Russia's chip industry has been stemmed.

By Otis Port in Zelenograd and Peter Galuszka in Moscow

Where to find a plane.

Where to find your bags.

Where to find a taxi.



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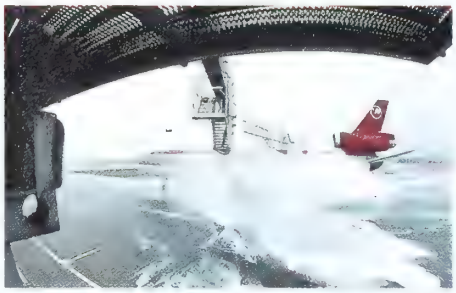
Developments to Watch

EDITED BY PETER COY

TO DE-ICE OR NOT TO DE-ICE?

WHEN THIS PAST WEEK'S mammoth blizzard blanketed airports from Washington to Boston, canceling flights was an easy call. In lesser storms, however, decisions on whether to ground planes or de-ice them instead aren't so simple. One problem, says Roy M. Rasmussen, manager of the ground de-icing program at the National Center for Atmospheric Research (NCAR) in Boulder, Colo., is that airports may base the decision on snowfall rates, gauged by visibility. That's a poor indicator of whether snow on the aircraft will actually turn to ice, he says.

In a study supported by the Federal Aviation Administration, Rasmussen recently found that the amount of water in the snow is a better predictor. With colleagues at NCAR, he developed a system to monitor it. The



system, which is undergoing trials at O'Hare International Airport in Chicago, uses five gauges at and around the airport to continuously measure snowfall rate and water content. A workstation correlates this information with wind, temperature, humidity, and radar data from weather stations and displays the results—current conditions and 30-minute predictions—on video monitors. Rasmussen figures that the system would cost airports $50,000 to $100,000 to install.

A WAY TO MINE SILVER FROM OLD X-RAYS

THOSE OLD X-RAYS OF YOUR cracked bicuspids are a great source of silver. Processors usually burn X-ray film and retrieve silver from the ashes or bleach the film and extract silver from the liquid by electrolysis. But burning requires a furnace with costly pollution controls, and bleaching produces chemical byproducts that must be treated. A Japanese chemical engineer says he has a better way: enzymes from bacteria.

Haruo Ishikawa and his colleagues at the University of Osaka Prefecture use alkaline protease enzymes produced by the B21-2 species of *Bacillus* bacteria.

Short strips of used film are mixed with the protease in a reactor under conditions that are alkaline—that is, the opposite of acidic. The enzyme breaks down the film's gelatin layers, freeing the fine particles of silver. A coagulant such as aluminum sulfate makes the silver grains precipitate out of the solution.

Ishikawa says he expects that Japan Chemical Engineering & Machinery Co. will build a pilot plant in Osaka within two years and process more than 2,000 pounds of used X-ray film per day.

MONITORING ASTHMA VIA MODEM

THE NUMBER OF SERIOUS complications from asthma—including deaths—has risen some 40% in the past decade. One reason: Many patients don't take their medicine regularly and wait too long to report symptoms. Constant monitoring of lung function would help keep asthmatics out of emergency rooms, but that's expensive and impractical.

ENACT Health Management Systems in Mountain View, Calif., hopes to help matters with a pocket-size airway monitor called AirWatch. AirWatch records how hard and how much air a patient can blow. Hooked to a telephone jack, AirWatch transmits its data to a central computer. Within minutes, a report is faxed to a physician's office. Each month the doctor and patient receive a summary that charts compliance and provides information on how the asthma is responding to medication.

The device is for children age 5 and up as well as adults. It costs about $50, and a hookup to the computer costs $100 a year. Several hundred doctors already use the system, and a few insurance companies have covered the costs.

INNOVATIONS

■ The pigment that makes pepperoni pink may soon help preserve processed meats by slowing oxidation. Fereidoon Shahidi, a food biochemist at Memorial University of Newfoundland, is seeking Canadian approval for use of the pigment, which can be derived from red blood cells, as an alternative to nitrite curing. Nitrites can react to form traces of cancer-causing nitrosamines in meat.

■ A new blend of glass can hold dissolved plutonium equal to 7% of its weight without deteriorating, say researchers at Argonne National Laboratory in Illinois. In tests of its suitability for storing radioactive wastes, the alkali-tin-silicate glass stood up to hot vapors that simulated thousands of years of natural degradation.

■ Israel's Electric Fuel Corp. is moving closer to showing that zinc-air batteries can power electric vehicles. Instead of trying to recharge them, which doesn't work well, Electric Fuel dismantles them and replaces the oxidized zinc with fresh metallic zinc. It recently finished a plant in Bremen, Germany that will serve German Postal Service vehicles.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwjan@businessweek.com

ECHNOLOGY

THE GAME'S AFOOT -AND IT'S MARKETING

lympic sponsors spend big to promote high-tech offerings

et the marketing games begin. As athletes around the world enter the final months training for the Olympic ames in Atlanta this summer, selling marathon is already ell under way. With 10,000 lympians competing in 271 vents at 27 venues, and with 5,000 reporters and 2 million sitors looking on, the logistical ırdles of disseminating infor- ation and providing security the Olympics will be as high any in industry. For the com- anies that are volunteering the echnology that will do every- ing from time races to trans- it scores to publish the results, ıe games are a great opportu- ty to woo new customers.

The Olympics have always ıd a healthy dose of marketing ype, with companies paying a w million bucks for the right slap the Olympic rings on verything from beer mugs to ttons. But this time around, a ndful of technology companies e donating upwards of $40 illion in goods and services ch—10 times the going spon- rship rate at the Los Angeles mes. And they're not just do- ating Olympic track suits. hey're providing the sophisti- ted data, communications, and ecurity systems that will back ıe Atlanta games. To make the ost of that investment, the do- or companies are using the orld's biggest sports event to owcase cutting-edge technology to otential customers, who are already rriving in Atlanta by the planeload.

IBM signed on as an Olympic partner create an information infrastructure at will connect athletes, visitors, and edia worldwide. The centerpiece is a coring system that will tally scores, eyed in from pen-based laptops at each enue, and feed them to the world's ress in seconds. IBM kiosks scattered roughout the Olympic Village will give officials, athletes, and coaches access to 60 gigabytes of data—everything from athlete biographies to restaurant picks.

Performing right alongside the IBM technical folks in Atlanta are teams of sales and marketing staff. "The Olympics mimic a client environment that has rigorous requirements, like tough deadlines and a huge scope," says Ronald Pamich, director of IBM's Olympic Games project. "We want our potential clients to leave the games and think 'How can this model work for me?'" Kent C. Nelson, chairman and CEO of United Parcel Service Inc., was treated to an evening of pre-Olympics gymnastics—and demonstrations of the kiosks and scoring system—at the Georgia Dome recently, courtesy of IBM. IBM didn't score any new UPS business, but it did get Nelson's attention. "We may be able to use something similar to IBM's games-management system to help us integrate all the information on the packages that we ship," he says.

HOT STOP. Xerox Corp. is using its sponsorship to vault into the $100 billion high-end publishing business. Its Olympic facilities will be able to print 135 pages a minute and will turn out bound volumes of scores and athlete information within three to 24 hours of an event for judges and journalists. "We want to be in this business and the Olympics will give us significant inroads. For us, the Olympics will be a proving ground," says Vince Schaeffer, Xerox's manager of Olympic programs. Xerox and AT&T have teamed up to create a mobile scoring center in a 48-foot trailer. The Olympics Technology Trailer Operation, or OTTO, has already hit the road and serviced pre-Olympic events. It has also been a favorite stop on sales tours.

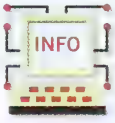
Some smaller companies are hoping the Olympics will catapult them into the big leagues. Sensormatic Electronics Corp., a $920 million company in Deerfield Beach, Fla., that makes plastic garment tags used to deter shoplifters, bought in as a $20 million sponsor. It will provide athletes and officials with microchip-embedded badges that will whisk doors open as wearers approach and scanners that will read handprints to match the badges with those wearing them. For the past year, Sensormatic has been flying three or four clients a week to Atlanta to tour security installations. Louis Chiera, director of Olympic marketing, says the sponsorship has brought in $10 million in sales so far. And there are still nearly six months to go before the torch enters the Olympic stadium—time for technology sponsors to win plenty of gold in Atlanta.

By Nicole Harris in Atlanta

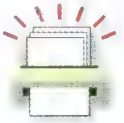
OVERVIEW: *Sensormatic's camera scans the stadium*

The Olympic Efforts You Don't See

Sponsors are donating technology to the Atlanta games, but the real game is showing it off to potential customers.



IBM Information infrastructure. Includes three mainframe computers, 80 midrange computers, and 6,000 workstations.



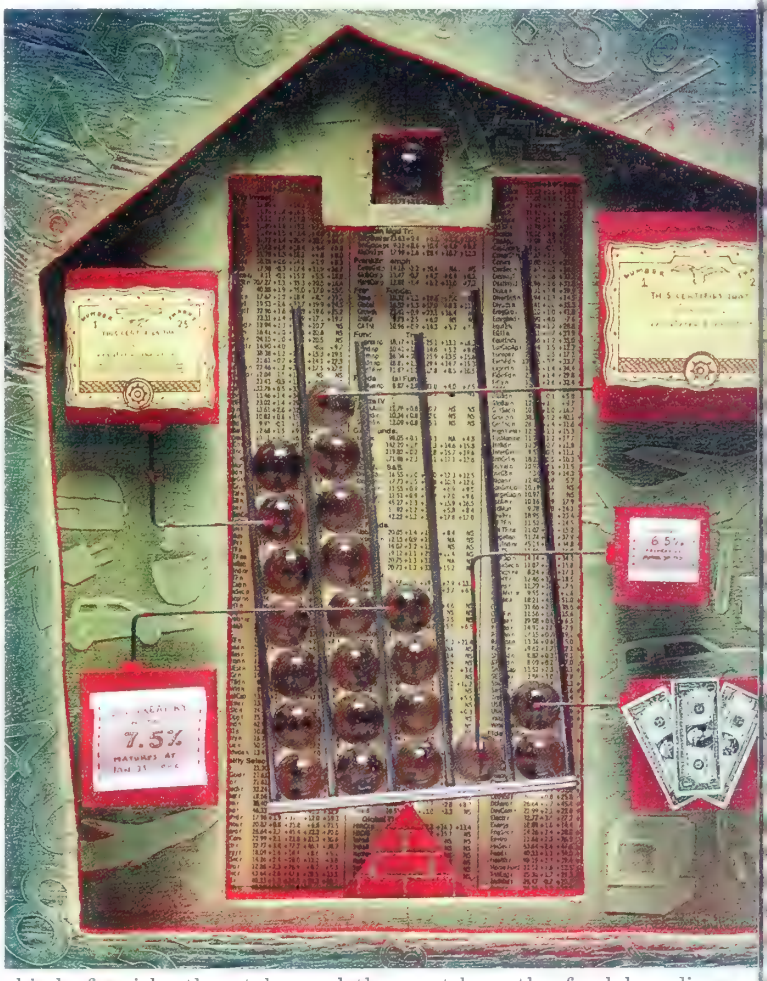
XEROX Printed scores. Will provide equipment including more than 100 laser printers, 1,000 copiers, and four publishing systems.

MOTOROLA Digital radio system to support transportation, security, and event management. Includes 10,000 portable radios, 6,000 pagers, 1,200 cellular phones, and 1,500 computer modems.

AT&T Telecommunications. Includes long-distance voice and data services, 24-hour telephone-based translating services in 140 languages, and telephone devices for the hearing-impaired.

EDITED BY AMY DUNKIN

THE NO-SWEAT FUNDS YOU SHOULD WORRY ABOUT



Are you scared that the sky-high stock market might tumble and take your investments down with it? Mutual-fund salespeople have an antidote for your worries: asset allocation funds. After all, asset allocation funds—which are diversified mixes of stocks, bonds, and money-market instruments—survived the 1987 stock-market crash and earned solid returns for the year.

But investing in a fund today based on what it did back in 1987 is foolhardy. For starters, the market conditions are quite different. In 1987, these funds did well because as stocks melted down, the bond market rallied, and this helped to offset the losses. But now, bonds and stocks are both high: Chances are, if one tanks, so will the other. Even more important, very few of the asset allocation funds around today were in business back then. In fact, 165 of the 236 funds tracked by Morningstar Inc. are less than two years old, and whether they could survive a crash is anybody's guess.

HOLD THE HASSLE. That said, asset allocation funds can still be good choices for those who want to diversify beyond stocks. They're often presented as options in 401(k) plans, too, and are appropriate for participants who are new to investing and who are without a portfolio large enough to diversify on their own. And even investors who have enough money to come up with their own asset allocation plan may not want to bother. As a group, asset allocation funds haven't fared badly: For the five-year period ending Dec. 31, 1995, they returned 11.75%, compared with 16.64% for U.S. diversified equity funds and 8.36% for taxable fixed-income funds, according to Morningstar.

INVESTING

But many mutual-fund investors have little to gain from asset allocation funds. If you have a long-term investment horizon and the stomach for stocks, there's no reason to own these funds. If you have a portfolio of several different funds, you may already own what the asset allocation managers are trying to provide you. They'll jiggle those assets around more than you will—but all this "fine-tuning" runs up expenses and doesn't necessarily deliver better returns. If you don't have that kind of portfolio, it's not hard to assemble one. You'll need about $10,000, since many such funds have minimums of $2,000 or $2,500. As for allocation ideas, you can use a shareholder report from one of the asset allocation funds as a road map.

If you do opt for the one-stop shopping offered by asset allocation funds, you still have to do some homework. The funds vary greatly in their investment styles, the risks they take, and the returns they earn. For instance, some invest in foreign securities, others don't. Some allow managers wide discretion in the amount of money allocated to any one asset, while others set minimum and maximum allocations.

GONE AWRY. The best barometer of a good asset allocation fund is dependability. What can you normally expect from the fund? Check the prospectus for the "neutral mix," or the expected average allocation. Then, find out how often and for how long the fund has diverged from that mix—and with what results.

The neutral mix doesn't mean much if the fund manager has the latitude to go astray. For instance, the prospectus of Dean Witter Managed Assets said that the fund sought total return among equities, fixed-income securities, and money-market instruments. Yet for most of 1995, in the face of the strongest stock market in 2 years, the fund was 100% in cash. Why pay Dean Witter a 1.77% expense ratio when

ou could have kept all your oney in a money-market nd for a mere fraction of at and perhaps earned a etter return? Fortunately, vestors can't stumble into ean Witter Managed Assets aymore. The management mpany recently merged it to the better-performing ean Witter Strategist fund, records among its peers, is a case in point. The fund built its record by making some extreme bets, such as emerging-market debt. For instance, the fund was up 23.3% in 1993—twice the return of the Standard & Poor's 500-stock index that year—only to plunge with the peso to a –6.6% return in 1994. "The fund's manager [Bob Beckwitt] is a real quant guy who got blindsided," says Jane King, president of Fairfield Financial Advisors in Wellesley, Mass. Humbled, the fund now takes a more defensive posture—cutting back exposure in emerging markets to less than 5% and holding more in cash—and it produces less exciting but ultimately more dependable returns. In 1995, for instance, Asset Manager earned an 18.16% return.

It's one thing to diversify a portfolio, but quite another to try and "time" markets. If an asset allocation fund is making dramatic swings among various asset classes, it may be trying to do just that. Ideally, managers should make changes in their allocations gradually, not abruptly. Is the fund engaging in market timing? Check its historical weightings through one of the independent mutual-fund rating services, such as Morningstar. A high turnover (one in excess of 150%) and shifts between asset classes (plus or minus 20% in a year) are red flags: The fund is an aggressive timer and should be avoided.

Theoretically, you should also be able to glean this information through a simple telephone call to a fund's shareholder representative, according to Albert J. Fredman, professor of finance at California State University at Fullerton and the co-author with Russ Wiles of *Building Your Mutual Fund Portfolio* (Dearborn Financial Publishing, $19.95, 800 829-7934). But a few calls to several important fund companies' 800 numbers proved otherwise. The rep at Blanchard funds had never heard of a neutral mix and, when asked for the fund's turnover, was able to give numbers only through Apr. 30, 1995, although the request was made on Nov. 28. Even the more well-informed reps at Fidelity Investments could report only two-month-old turnover figures for their asset allocation fund. While you may not be able to get the most current numbers, check a fund's annual report to get a handle on the outfit's management style. The timeliness of the information varies. Performance and expense ratios are current, while the turnover and specific portfolio holdings are reported less frequently.

HAMMERED BY FEES. Because asset allocation funds trade a lot, their brokerage costs tend to be higher, something not always reflected in a fund's expense ratio. But such costs nip into the return, says financial planner Mark Bell of Chicago's Mark Bell & Associates. "High fees are a tough benchmark for any fund manager to beat," says consultant Derek Sasveld of Ibbotson Associates, who recommends an expense ratio no higher than 1%.

Of course, a slightly higher expense ratio is not a problem if you have an excellent portfolio manager. Find out what kind of experience particular managers have in different asset classes by calling the fund company or rating service. If they are known solely for U.S. equities, find out who's managing the bond or foreign portions of the portfolio. For instance, the lead manager of the Strong Asset Allocation Fund is Brad Tank, who also heads the firm's taxable fixed-income department. While Tank has final investment veto power, the fund benefits from the input of three other fixed-income managers and four equity managers. As of Dec. 31, its one-year total return was 21.96%.

It's also a good idea to invest in an asset allocation fund that can be run with in-house skill. Blanchard Global Growth, for instance, pays five different subadvisers to run various portions of the fund. That high overhead results in an enormous 2.5% expense ratio and substandard returns.

Sure, you can find asset allocation funds with solid performance and reduced risk. But for a category that's sold as a convenience, an awful lot of diligence is required to make sure that a fund meets an investor's asset allocation needs. *Kerry Capell*

Asset Allocation Funds Vary Widely

:TIVE	1-YR TOTAL RETURN*	EXPENSE RATIO	TURNOVER
IARD GLOBAL GROWTH s long-term capital appreciation ed to allocate 0%–65% to U.S. and foreign bonds, or precious metals; 0%–15% to g-market securities; and 0%–100% to cash	12.71%	2.51%	221%
Y ASSET MANAGER for reduced risk over the long term ed to allocate 10%–60% to stocks, 20%–60% s, and 0%–70% to short-term fixed income wn options, futures, warrants, or emerging- securities. No limit on foreign investments	18.16	0.97	137
URSA s results that correlate inversely e S&P 500 s no stock, bonds, foreign securities, or gold. , just options on securities and stock indexes, contracts, and U.S. Treasury securities	–20.15	1.39	0**
S ASSET ALLOCATION s high total return ed to allocate 10%–60% to stocks, 20%–60% ds, 0%–100% to cash, and 0%–100% to foreign securities	21.95	1.26	327
IRD ASSET ALLOCATION ested in achieving highest possible return ed to allocate 0%–100% to domestic stocks, and money-market instruments	35.46	0.49	34

'31/95 **Turnover not measurable for securities with maturities under one year DATA: MORNINGSTAR INC

ereby managing to bury e dismal record.

Although such extreme alcations are by no means the orm, they are troubling. /ith most mutual funds, such s an international bond fund a domestic small-company nd, the manager is required have at least 65% of the oney in those sorts of ass or in cash. With asset llocation funds, however, ou're never quite sure here your money is.

The $11 billion Fidelity Asset Manager Fund, which has ne of the better track

MERGER MODE: *The trend likely won't end till just 10 or 15 giants remain*

DRUG STOCKS TO WATCH IN '96

If you were looking for market action in 1995, pharmaceutical stocks were just what the doctor ordered. U.S. health-care reform died, and with it fears that drugmakers would see their revenues sharply limited. Plus, widespread cost-cutting in the industry helped turn profits around after a slump in 1994. The sector also saw a wave of megamergers, starting with the $14 billion combination of Britain's Glaxo and Wellcome in January and winding up with the widely praised marriage of Sweden's Pharmacia and the U.S.'s Upjohn.

SMART MONEY

HEADY RETURNS. All that news pushed global pharmaceutical stocks through the roof: In the U.S., the group outperformed the Standard & Poor's 500-stock index by 18 percentage points, and in Britain, the pharmaceutical sector returned 19 percentage points more than the benchmark *Financial Times*-Stock Exchange 100 index.

That's a tough act to follow, but some experts think more gains could lie ahead. The difference this year, says Richard Vietor, a first vice-president at Merrill Lynch in New York, is that "earnings growth will shift from cost-cutting to fundamentals." That means investors may want to focus on companies with significant new products.

In the U.S., Merck's Fosamax, an osteoporosis treatment, and antihypertensive Cozaar both received Food & Drug Administration approval in 1995 and are getting positive early reports. Pfizer is expected to launch four drugs from 1996 to 1998, including Zyrtec, a low-sedating antihistamine that received FDA approval last month. Such innovations are expected to push their creators' earnings growth rates above the average 7%-to-10% that is being forecast for the industry in 1996.

In addition, while the pace of consolidation is bound to slow—if only because fewer takeover candidates remain—the merger trend among drug companies isn't over. Glaxo Wellcome, the world's biggest drugmaker, still has only 6% of the global market. So, many industry watchers expect combinations to continue until only 10 or 15 giants are left. Among American takeover targets, the biggest unknown remains closely held Warner-Lambert. Its shares are up nearly 14% since July, despite a forecast earnings decline for 1996, on merger speculation.

Takeover plays aside, analysts believe that there are enough drug stocks with upside potential left to build a healthy portfolio. Switzerland's Sandoz is widely recommended as it continues to divest noncore assets—"changing its spots and focusing on what it does best," says Salomon Brothers analyst Peter Laing. Also, Sandoz' pipeline includes the Alzheimer's drug Exelon, for which the company is expected to seek FDA approval by the end of 1996.

Sweden's Astra also gets high marks, in part because its stock is relatively inexpensive. "Astra looks like one of the most undervalued [drug] companies in Europe," says Kevin Scotcher, who follows the pharmaceutical industry for Kleinwort Benson in London. Its projected price-earnings ratio of 2 compares with a starry 37. for industry highflier Roche. Another plus: The patent for Losec, Astra's ulcer medication, doesn't expire until 2004—six years after the first patent on Glaxo Wellcome's competing drug, Zantac, runs out.

SLEEPERS IN JAPAN? Although most investors have chased the hot transatlantic drug-industry action, some stock-pickers think the real sleepers are in Japan. Samuel Isaly, manager of Capston Medical Research Fund and a partner at industry analysts Mehta & Isaly, believes that "Japanese pharmaceuticals are very attractively valued and will lead performance of the sector in 1996."

One pick is Sankyo, whose cholesterol-busting Pravachol was found to reduce mortality in long-term studies and already has posted worldwide annual sales of $1.1 billion. Its price-earnings ratio of 26 is not much higher than that of Western competitors—and much lower than Japan's average p-e of 50.

As drug-stock fever spreads around the world, investors will have every reason to view the lofty prices of drug stocks with caution. But if the pundits prove correct, megamergers and new products should keep the sector sizzling for some time. *Joan Warner and Heidi Dawley*

Take Two and Call Us In 12 Months

COMPANY		PRICE ON JAN. 8	P-E RATIO*
SANDOZ**	Alzheimer's drug in pipeline	$46	19.4
MERCK	Two new products spell growth	64	24.0
ASTRA**	Good value among the Euros	42	20.0
PHARMACIA-UPJOHN	Continuing benefits from merger	38	17.8
SANKYO	Creator of top-selling Pravachol	23	25.8

*On estimated 1996 earnings per share **ADRs DATA: BUSINESS WEEK, BLOOMBERG FINANCIAL MARKETS

MUSIC TO YOUR EARS -AND EYES

ENTERTAINMENT

t first glance, there's othing unusual bout *Stripped*, the atest Rolling Stones elease on compact disk. It oks like an ordinary disk, sts about ie same, id lets fans relish 14 classic ngs when spun on a CD ayer. Yet Stones addicts ho pop the Virgin Records elease into a CD-ROM drive i their personal computer 're treated to something ore: on-camera interviews ith Mick Jagger and Keith ichards, plus several inutes of music videos.

Stripped is an example of a dding digital format called e enhanced CD, a cross beween audio-only compact sks and CD-ROMs that hold ultimedia sizzle but don't ay on your stereo. Some 0 enhanced CD titles eached consumers around hristmastime, and there are ore on the way, covering erything from alternative ck to classical. Mariah arey, Todd Rundgren, and undgarden are among the ck and pop artists who ve come out with enhanced s—some with music videos, teractive games, and even direct links to the performer's Web sites. On the classical side, there are enhanced CDs devoted to Chopin, Mozart, Tchaikovsky, and others. Music Pen developed the 35-disk LaserLight series of classical recordings, which lets listeners follow the score on-screen or see notes and videos on the composers. And Graphix Zone unveiled an enhanced CD tagged to director Oliver Stone's *Nixon*. In its audio CD mode, you get the John Williams movie soundtrack. The multimedia portion has the film's trailer, plus interviews with Stone and Williams.

As with regular CDs, enhanced versions often offer a compilation of many entertainers. Compton's NewMedia joined Rhino Records on *Rock Expedition: The 1960s* (with the Monkees and Sonny & Cher, etc.) *Spew+* on the Atlantic Recording features a "digizine," where viewers can watch full-screen videos of the nine new performers whose music is on the disk.

Few enhanced CDs are as peculiar as *SuperModels in the Rainforest* from Virgin Interactive, which also features a variety of artists. On the audio side, people can listen to music from Duran Duran and Soul II Soul. But in its multimedia pose, *SuperModels* is a cross between *Sports Illustrated*'s annual swimsuit issue and a project worthy of the World Wildlife Fund. As its title suggests, *SuperModels* makes a blatant attempt to attract men by showing off scantily clad women photographed in the Costa Rican tropics. But the disk also emphasizes a serious environmental mission, featuring colorful videos of animals and dignified discussions on preserving the rain forest.

The enhanced CDs that seem to work best are the ones that deliver material enthusiasts can't readily find elsewhere. In *the cranberries: doors and windows*, from Philips Media, fans are able to peek at home videos of the band on tour, or they can travel to the Woodstock revival concert in 1994 and rock to the song *Zombie*. *Bob Dylan's Greatest Hits Volume 3* on Columbia is an interactive two-disk set with a rich multimedia database. Under "catalog," Dylan devotees can click on old album covers to see song lists and liner notes. In "discography," diehards can hear 15-second audio clips from every song on selected albums.

When played on a PC, enhanced CDs add video sizzle to stereo sound

Enhanced CDs may not appeal to the casual fan, however. It's one thing to come home from a long day at the office, pop a CD into the stereo, and chill to the music. It's another matter to spend lots of time interacting with the performers. Nor is it clear that many people will pay a premium for enhanced disks: Some cost $5 to $6 more than regular CDs—although that's still well below most CD-ROMs. But even on a no-extra-cost title such as *Stripped*, some of the bonus material is just a teaser to get people to buy the $30 Stones *Voodoo Lounge* CD-ROM—*Stripped* has highlights from *Voodoo Lounge*.

OUT OF SYNC. Moreover, there are technical snags. With some enhanced CDs, you'll have to skip track one manually when playing the disk on an audio CD player, lest noise from the computer data stored on that track damage your speakers—or ears. That's a hassle for those who like to play songs in random order. And, as with many CD-ROMs, enhanced CDs don't always run as smoothly as you would like. For example, the videos on *Stripped* were out of sync on the 486-based PC I used.

Worse, many enhanced CDs won't perform on your CD-ROM drive at all. These include the old single-speed drives as well as other models. *Stripped*, among others, carries the disclaimer: "Warning: incompatible with some NEC drives and Mac PCI bus." *Billboard* estimates that as many as half of the installed drives won't handle the disks, but most hardware that has been bought in the past year or two should be O. K. Sony Music is shipping software drivers from Corel in its enhanced CDs (of a type called CD Plus), to allow certain CD-ROM drives to recognize the format. If that fails, you can always call up technical support. Then again, that may hit a sour note that could leave you pining for a reliable old CD. *Edward Baig*

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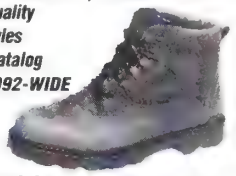

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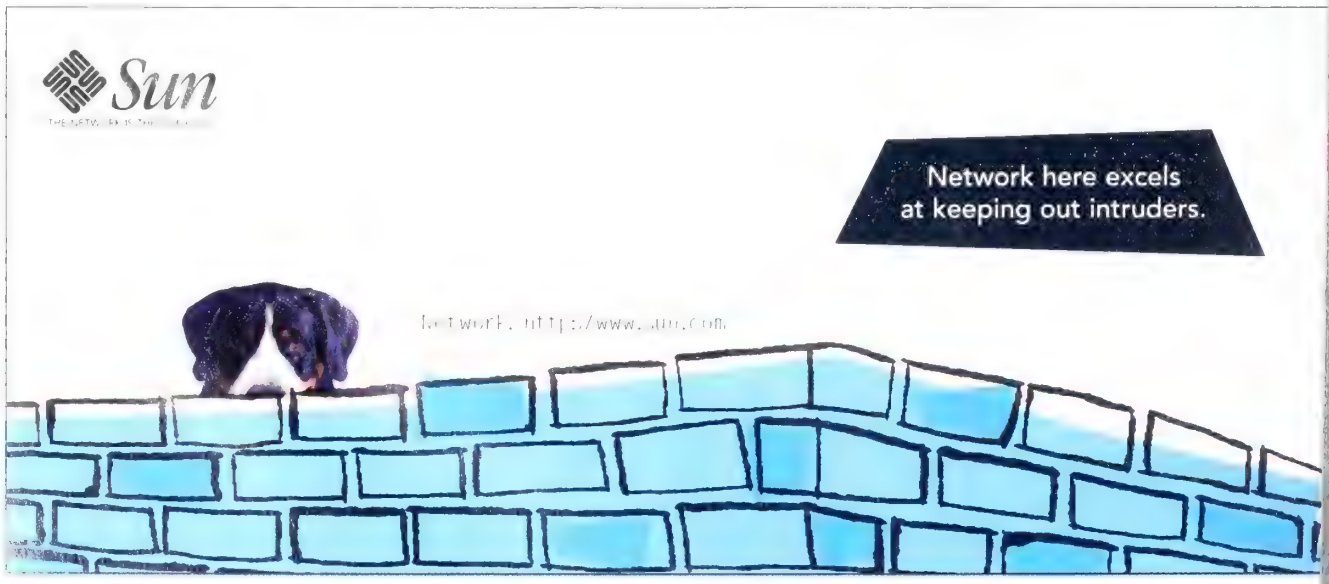

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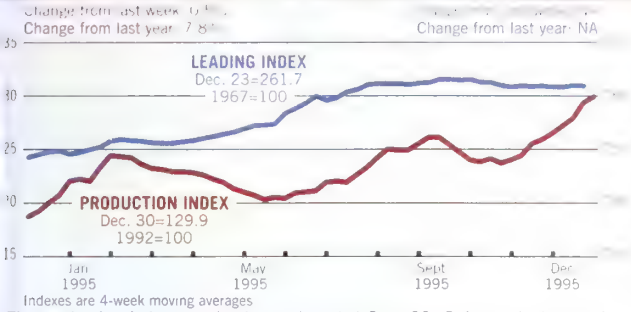

Indexes are 4-week moving averages

The production index rose in the week ended Dec. 30. Before calculation of the four-week moving average, the index fell to 130.1, from 131.4. Auto and truck plants were closed for the holidays, which in turn hurt rail-freight traffic. For the month of December, the index increased to 129.9, from 126.1 in November.

The leading index was not available for the latest week. The government shutdown and the blizzard prevented data from being collected.

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PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (1/6) thous. of net tons	1,951	1,818#	-1.7
AUTOS (1/6) units	92,978	0#	-15.0
TRUCKS (1/6) units	80,957	0#	-4.7
ELECTRIC POWER (1/6) millions of kilowatt-hrs.	NA	61,845#	NA
CRUDE-OIL REFINING (1/6) thous. of bbl./day	NA	13,990#	NA
COAL (12/30) thous. of net tons	14,785#	19,239	-7.9
PAPERBOARD (12/30) thous. of tons	NA#	839.4	NA
PAPER (12/30) thous. of tons	NA#	820.0	NA
LUMBER (12/30) millions of ft.	213.8#	423.0	-30.8
RAIL FREIGHT (12/30) billions of ton-miles	18.4#	24.4	-5.6

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA[1], SFPA[2], Association of American Railroads

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (1/5) S&P 500	NA	614.72	NA
CORPORATE BOND YIELD, Aaa (1/5)	NA	6.76%	NA
INDUSTRIAL MATERIALS PRICES (1/5)	NA	111.4	NA
BUSINESS FAILURES (12/29)	NA	NA	NA
REAL ESTATE LOANS (12/27) billions	NA	$502.3	NA
MONEY SUPPLY, M2 (12/25) billions	NA	$3,744.5	NA
INITIAL CLAIMS, UNEMPLOYMENT (12/23) thous.	NA	NA	NA

Sources: Center for International Business Cycle Research (CIBCR), Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans.

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/10) $/troy oz.	400.000	393.400	6.5
STEEL SCRAP (1/9) #1 heavy, $/ton	139.50	135.00	-3.1
COPPER (1/6) ¢/lb.	126.2	130.6	-9.8
ALUMINUM (1/6) ¢/lb	79.3	79.8	-17.9
COTTON (1/6) strict low middling 1-1/16 in., ¢/lb	80.49	79.47	-6.5
OIL (1/9) $/bbl.	19.95	19.81	14.5

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (1/9)	5.28%	6.06%	5.44%
COMMERCIAL PAPER (1/10) 3-month	5.45	5.50	6.18
CERTIFICATES OF DEPOSIT (1/10) 3-month	5.44	5.44	6.18
FIXED MORTGAGE (1/5) 30-year	7.30	7.40	9.39
ADJUSTABLE MORTGAGE (1/5) one-year	5.56	5.63	6.85
PRIME (1/10)	8.50	8.50	8.50

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/10)	105.21	104.42	99.88
GERMAN MARK (1/10)	1.44	1.44	1.54
BRITISH POUND (1/10)	1.55	1.55	1.56
FRENCH FRANC (1/10)	4.93	4.92	5.30
ITALIAN LIRA (1/10)	1572.0	1572.6	1624.0
CANADIAN DOLLAR (1/10)	1.36	1.35	1.41
MEXICAN PESO (1/10)[3]	7.525	7.575	5.725

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart), other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value. NA=Not available. r=revised. NM=Not meaningful

THE WEEK AHEAD

Due to the prolonged Washington shutdown, all government release dates are certain to be rescheduled.

INDUSTRIAL PRODUCTION

Wednesday, Jan. 17, 9:15 a.m. ▶ Output at the nation's factories, mines, and utilities probably rose 0.2% in December, according to the median forecast of economists surveyed by MMS International, one of the McGraw-Hill Companies. Production increased 0.2% in November. Unusually cold weather in December probably boosted energy output. The average industrial operating rates probably slipped to 83% last month, from 83.1% in November and 85.1% a year ago.

BUSINESS INVENTORIES

Wednesday, Jan. 17, 10 a.m. ▶ Inventories held by manufacturers, wholesalers, and retailers likely rose by about 0.4% in November, on top of a large 0.6% increase in October. Business sales probably rose 0.5% in November after dropping 0.4%. That's suggested by the already-reported 0.8% jump in retail sales.

BEIGE BOOK

Wednesday, Jan. 17, 12 noon ▶ The Federal Reserve's survey of its 12 districts—the so-called beige book—catalogs anecdotal reporting on business conditions across the U.S. The roundup is prepared a few weeks before each policy meeting. In the Dec. 6 beige book, the Fed said that economic activity continued to expand, "but at the somewhat slower pace reported in the last beige book." In addition, the report noted that labor shortages were lifting wages in some areas.

HOUSING STARTS

Thursday, Jan. 18, 8:30 a.m. ▶ Housing starts probably rose to an annual rate of about 1.4 million in December. That's suggested by the month's increase in mortgage applications for home purchase, as compiled by the Mortgage Bankers Assn. Starts fell 3.7% in October, to a 1.34 million pace, but because of the shutdown, November starts have yet to be reported.

This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

BusinessWeek ONLINE

Sunday

Scott McNealy has made Sun Microsystems the hottest company in network computing and one of the hottest anywhere in high tech. Here's your chance to talk with Sun's CEO about how he did it (his motto: "Kick butt and have fun") –and what's next. He will be online with BW's Rob Hof, author of the current issue's Cover Story on **Sun. Jan. 14 9 p.m. EST in the Globe**

New Look

Now there's a new reason to sign up for America Online: BW Online's redesigned screens, making it easier than ever to find the entire contents of every issue and all the other online features, including the Best B-Schools, Message Boards, the BW Online Store, and much more.

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

For a free trial diskette including 10 free hours on AOL, call 1-800-641-4848 and mention Business Week.

AMERICA Online

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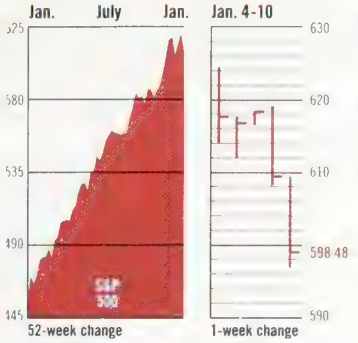
Business Week (ISSN 0007-7135) published weekly, except for one issue in January, by The McGraw-Hill Companies, Inc. Executive, Editorial, Circulation, and Advertising Offices: 1221 Avenue of the Americas, New York, N.Y. 10020. U.S. subscriber rate $49.95/year; Canada: CDN $69/year. Second-class postage paid at New York, N.Y., and at additional mailing offices. Postage paid at Montreal, P.Q. Canada Post International Publications Mail Product Sales Agreement No. 246484. **Postmaster:** Send address changes to BUSINESS WEEK, P.O. Box 430, Hightstown, N.J. 085

Investment Figures of the Week

OMMENTARY

tters over the strength of earn-
igs sent tech stocks into a tail-
pin. Motorola's weak fourth-quar-
r earnings was fuel for the fire
nd the Dow Jones industrial index
ell almost 100 points on Jan. 10
end the week down 3%. There
as no joy in bondland, either: Re-
orts that talks to balance the
deral budget had broken down
nt prices plunging. That moved
e yield on the 30-year Treasury
nd up to 6.19%. Gold benefited.
hit the highest level in 2½ years,
rging above $400 an ounce.

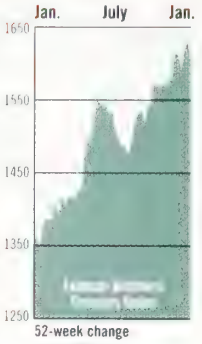
STOCKS



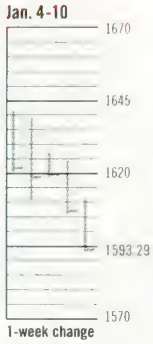
52-week change
+29.6%

1-week change
-3.7%

BONDS

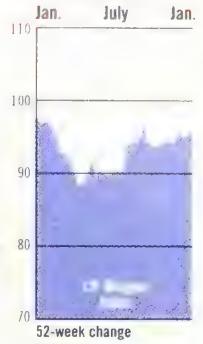


52-week change
+17.5%

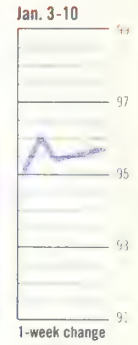


1-week change
-2.5%

THE DOLLAR



52-week change
-1.6%



1-week change
+0.6%

MARKET ANALYSIS

.S. STOCKS	Latest	% change Week	% change 52-week
)W JONES INDUSTRIALS	5032.9	-3.1	30.3
IDSIZE COMPANIES (S&P MidCap Index)	208.2	-4.5	22.6
MALL COMPANIES (Russell 2000)	302.9	-3.9	22.1
.L COMPANIES (Russell 3000)	340.2	-3.9	28.6

OREIGN STOCKS	Latest	% change (local currency) Week	52-week
NDON (FINANCIAL TIMES 100)	3671.5	-1.2	20.4
KYO (NIKKEI INDEX)	20,612.3	3.7	5.4
RONTO (TSE COMPOSITE)	4781.1	-0.8	14.2

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.17%	5.19%	5.75%
30-YEAR TREASURY BOND YIELD	6.19%	5.95%	7.84%
S&P 500 DIVIDEND YIELD	2.27%	2.21%	2.80%
S&P 500 PRICE/EARNINGS RATIO	16.9	17.6	17.0

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	562.8	559.9	Positive
Stocks above 200-day moving average	66.0%	69.0%r	Neutral
Speculative sentiment: Put/call ratio	0.67	0.53	Neutral
Insider sentiment: Vickers sell/buy ratio	1.33	1.29	Positive

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

NE-MONTH LEADERS	% change 1-month	12-month
DEFENSE ELECTRONICS	24.1	134.8
GOLD MINING	8.1	38.2
SHOES	6.3	31.6
ELECTRIC COMPANIES	6.0	23.9
REGIONAL TELEPHONE COMPANIES	5.6	43.8

Strongest stock in group	% change 1-month	12-month	Price
LORAL	25.7	134.7	44
NEWMONT MINING	17.3	54.2	52 5/8
REEBOK INTERNATIONAL	8.2	-28.0	28
SCECORP	13.5	18.2	17 7/8
NYNEX	10.6	41.2	52 1/4

NE-MONTH LAGGARDS	% change 1-month	12-month
SEMICONDUCTORS	-17.3	19.7
COMMUNICATIONS EQUIPMENT	-14.2	31.7
INSTRUMENTATION	-12.5	44.0
PERSONAL LOANS	-12.3	35.7
COMPUTER SOFTWARE	-12.2	33.1

Weakest stock in group	% change 1-month	12-month	Price
MICRON TECHNOLOGY	-32.7	71.5	36 7/8
DSC COMMUNICATIONS	-24.3	-17.2	28 3/8
TEKTRONIX	-21.4	23.8	43 1/2
HOUSEHOLD INTERNATIONAL	-12.9	46.2	55
AUTODESK	-15.8	-20.0	32

MUTUAL FUNDS

MORNINGSTAR INC.

ADERS

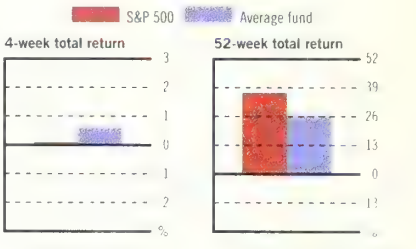
ur-week total return	%
WRIGHT EQUIFUND-MEXICO	17.3
MORGAN STANLEY LATIN AMERICAN C	12.2
T ROWE PRICE LATIN AMERICA	11.6

-week total return	%
ALGER CAPITAL APPRECIATION	73.7
PERKINS OPPORTUNITY	69.0
FIDELITY SELECT ELECTRONICS	65.6

LAGGARDS

Four-week total return	%
STEADMAN AMERICAN INDUSTRY	-15.6
STEADMAN TECHNOLOGY GROWTH	-12.9
ROBERTSON STEPHENS INFORMATION AGE	-12.8

52-week total return	%
EV MARATHON GREATER INDIA	-33.4
STEADMAN TECHNOLOGY GROWTH	-29.9
AMERICAN HERITAGE	-28.7



RELATIVE PORTFOLIOS

DRI/McGRAW-HILL

llar amounts represent the
esent value of $10,000
vested one year ago
each portfolio

rcentages indicate
e-day total returns

U.S. stocks	Treasury bonds	Foreign stocks	Gold	Money market fund
$13,546	$13,320	$12,320	$10,595	$10,564
-1.82%	-1.09%	+1.00%	+0.08%	+0.12%

data on this page are as of market close Wednesday, Jan. 10, 1996, unless otherwise in-
cated. Industry groups include S&P 500 companies only; performance and share prices are as of market close Jan. 9. Mutual fund returns are as of Jan. 5. Relative portfolios are valued as of Jan. 9. A more detailed explanation of this page is available on request. r=revised

NET CENSORSHIP IS INDECENT

The Internet is supposed to help set the world free. Borderless communication and the unfettered flow of data anywhere, anytime, promise to promote democracy and boost economic growth. All kinds of companies are making big plans to do business on the Net. Well... not so fast, folks.

CompuServe Inc. just pulled the rug out. When a prosecutor in conservative Bavaria recently launched an investigation of the online service company, holding it accountable for sites on the Internet that showed child pornography, CompuServe caved in with indecent speed. Without waiting for any charges actually to be filed by the German prosecutor, the company blocked access to 200 newsgroups (many of them having nothing to do with pornography) for all of its 4 million subscribers in 140 countries, including the U.S.

Now it appears that the lowest common denominator of censorship might prevail on the Net. Material might have to conform to all notions of moral and political correctness. This will severely hurt cyberspace and limit its promise as a commercial vehicle. After all, there are countries where religion prohibits the paying of interest. Will conservative Oman be able to block business transactions on the Net in the U.S.?

At the core of the cyber-censorship debate is a fundamental distinction. Is the Internet—and services such as CompuServe that provide access to it—a common carrier such as a telephone company, or a broadcaster like ABC? Since the Net merely provides a depository for text, pictures, and sound rather than creating them, it is clearly a distributor. But that conclusion frustrates law enforcers. And not only in Germany. Several Asian governments are rushing to curb access to the Net. And in the U.S., the Exon Amendment to pending telecommunications legislation would make it a crime to knowingly transmit "indecent" materials over the Net.

The utopian promise of uncensored freedom on the Net is currently clouded by this specter of culture clashes. How to protect against child pornography or neo-Nazi propaganda is a serious concern, not to be dismissed out of hand by wired-up anarchists. Different communities on the Net have different customs and laws relating to privacy, intellectual property, and propriety. Pretending they don't won't work.

What is the solution? The CompuServes of the world need to move quickly to provide individuals and communities with simple electronic locks for Net materials deemed too violent, pornographic, or politically extreme. A number of software packages already do just that. In the U.S. and Europe individuals should be held responsible for screening what comes over the Net transom, not the government. The Exon Amendment, for all its good intentions, is as wrongheaded as the German state prosecutor's attack on CompuServe.

BREAK THE VICIOUS CYCLE WITH JAPAN

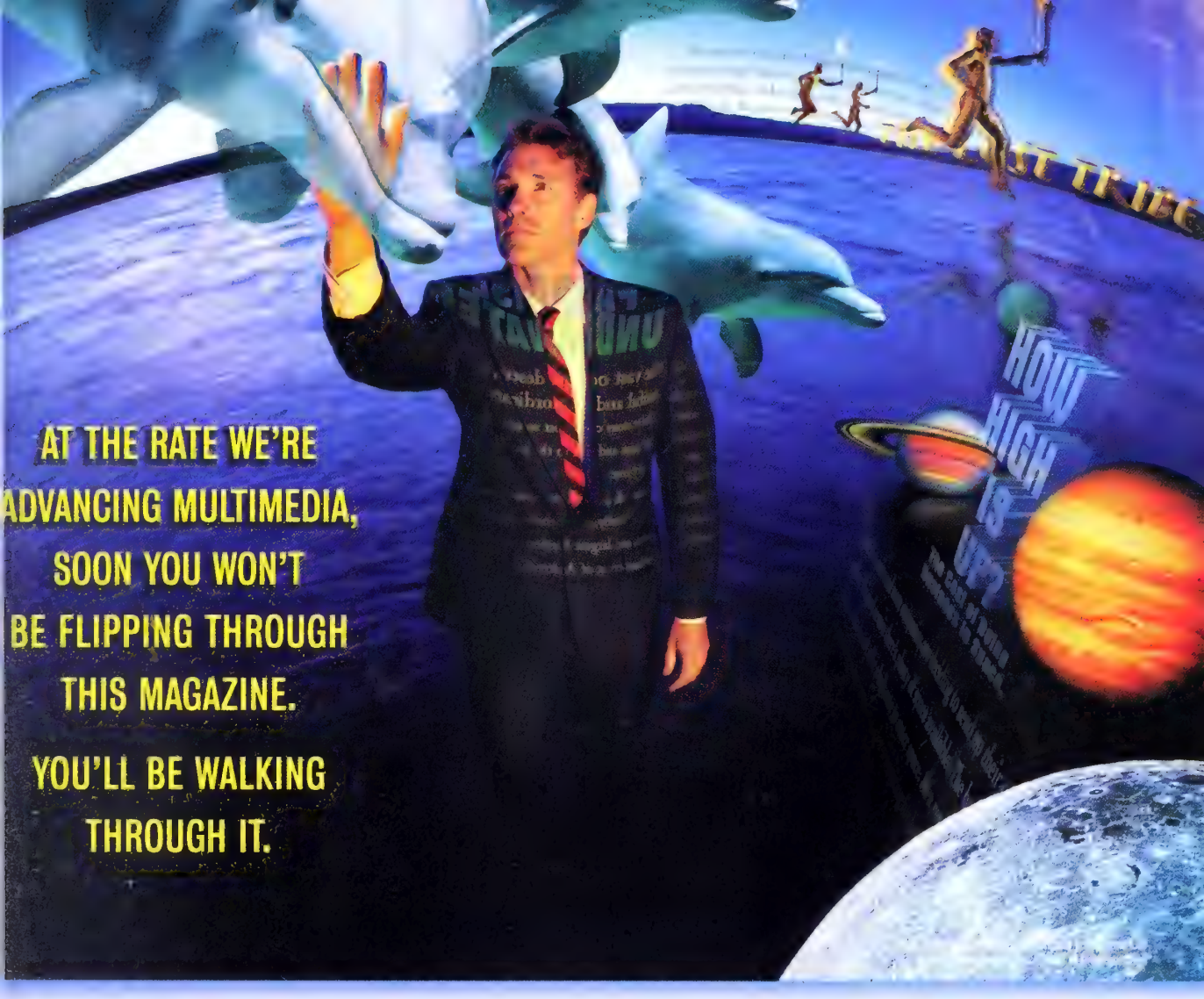
Washington policy toward Japan seesaws between foolish optimism and deep cynicism. Japan is perceived as either just about to become like the U.S.—an open, consumer-driven market economy that imports like crazy—or an intractably closed, bureaucratically controlled mercantilist society that runs huge trade surpluses with everyone. With the recent return to power of the Liberal Democratic Party and the appointment of Ryutaro Hashimoto as Prime Minister, this cycle is about to begin all over again. Alas.

Here's how it will unfold: President Clinton plans a trip to Japan in April. As the date nears, Washington will sound a chorus of hopeful notes. Hashimoto is seen as an outspoken "new generation" leader with Elvis-like sideburns. At the summit, a close Bill-Ryu relationship is ballyhooed to rival the Ron-Yasu tie between President Ronald Reagan and Yasuhiro Nakasone in the 1980s. Expect public bear hugs.

If history is any guide, some trade or investment dispute will then follow that proves frustratingly unsolvable. Despair will replace hope. Hashimoto will suddenly be remembered as the official who stoutly defied Washington in the auto talks. Whispering will begin about Hashimoto's close ties to Japan's bureaucrats and his party's long history of corrupt money-politics. U.S. cynicism about Japan will reemerge.

And then? The U.S. will look for another Japanese leader to pin its hopes on for change. Eyes are turning to opposition leader Ichiro Ozawa, head of the New Frontier Party. Ozawa says he favors cutting bureaucrats' power, slashing taxes, and wiping out special-interest loopholes. He will be seen in the U.S. as a reformist foil against Hashimoto in the 1996 Japanese general elections. Maybe he will be. But that optimism could quickly turn to disappointment. Ozawa was as much a machine-politician as Hashimoto before he turned reformer.

If the U.S. is to end its manic cycle of optimism and cynicism toward Japan, it must end its obsession with Japanese leadership. Washington must construct its own long-term post-cold war Japanese policy, replete with tactics. In economics, U.S. goals are already clear: open markets and balanced trade. But public shouting, private whining, and humiliating retreat hardly make for policy. The U.S. must find specific ways to work inside Japan, aligning with the corporate, political, and bureaucratic forces for deregulation and change. Finally, Washington must redefine its military relationship with Japan and relate it directly to U.S. economic security policies and goals. The failure to define and execute the right U.S. policy toward Japan, not the failure of Japanese leadership, is at the heart of America's frustrating relationship with the country. If the cycle of optimism and cynicism is to be broken, it is policymakers in Washington who must do



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How Far Will They Get?

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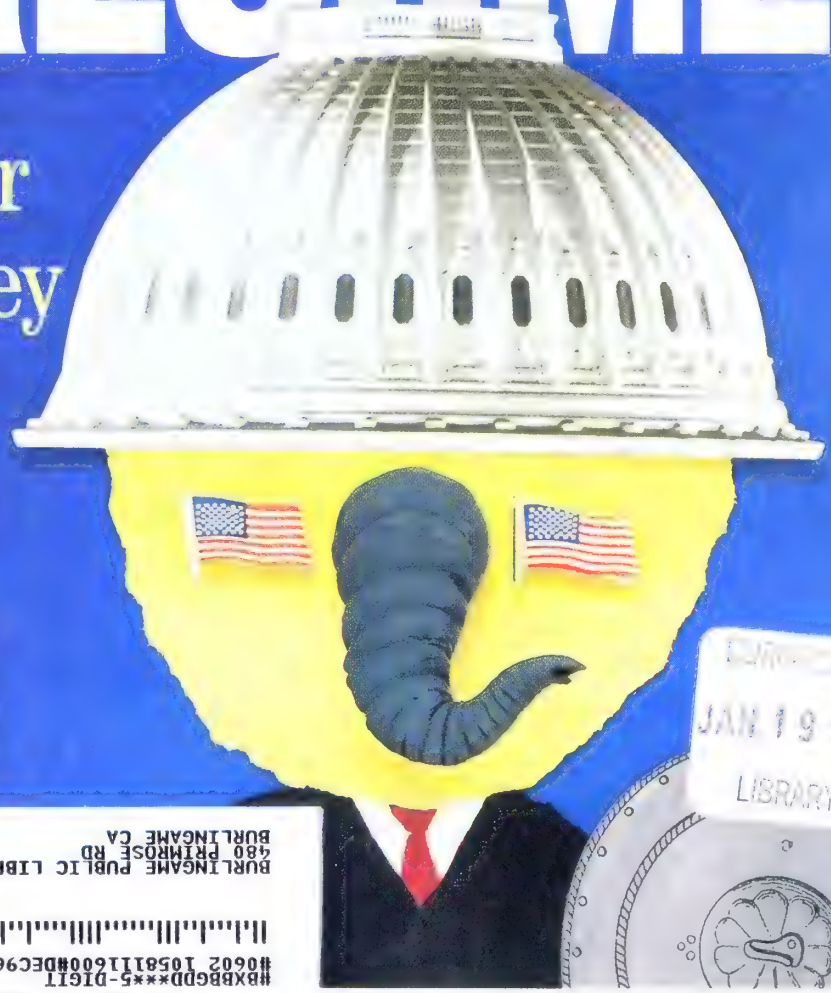

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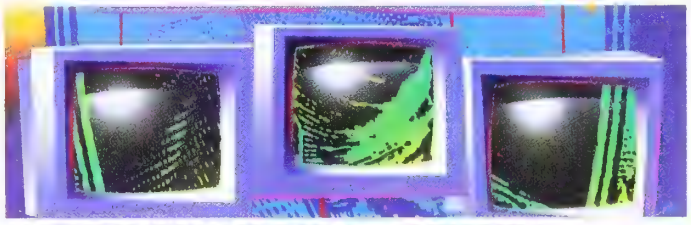

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Up Front

EDITED BY IRA SAGER, WITH OLUWABUNMI SHABI

TALK SHOW "A nation that routinely denigrates its public servants, and makes public service as unpleasant as possible, may soon find itself with the kind of government it has tacitly asked for." —*Alan S. Blinder, resigning as the Fed's vice-chairman*

GET SHORTY: *Thugs, plugs*

MAD AVE

GM MARKETING GOES SNAP, CRACKLE, POP

HOW MANY BOX TOPS WILL you have to mail in to get your next Olds? That's what wags are wondering now that General Motors has announced its first outside hires to be brand managers for GM vehicles. Michael McEnaney, 38, who headed Ralcorp Holdings' $350 million cereal and snack business, will go to work on Oldsmobile's Bravada sport utility and Silhouette minivan. In his old job, McEnaney was responsible for such brands as Chex cereal and once oversaw Tender Vittles and Purina Cat Chow. Meanwhile, the GMC truck division has hired Jeff Cohen, 36, from Nabisco, where he moved the cookie maker into Snackwell's breakfast bars. Cohen will manage the Jimmy sport utility.

The auto maker hopes the new managers—four more are to be named shortly—will inject a fresh perspective into GM's stuffy marketing. It's all part of a new strategy to market each GM car or truck individually, instead of positioning them en masse by division, like Olds or Chevy.

McEnaney will have to move fast. He's in charge of Silhouette, which was featured in the movie *Get Shorty*, where it earned the tongue-in-cheek sobriquet "the Cadillac of minivans." A new model is due this fall. Will it come with a secret decoder ring? *Kathleen Kerwin*

STREET NEWS

GOD HELP KMART... MAYBE HE DID

DID THE BLIZZARD OF '96 save Kmart from Chapter 11? The Jan. 8 East Coast storm prevented Standard & Poor's from meeting a deadline to downgrade Kmart's credit rating. S&P didn't lower $3.4 million in Kmart debt to junk-bond status until Jan. 12. Just a day earlier, the distressed discounter had cut a deal with creditors who could have forced it to redeem $550 million in bonds if its credit rating fell to junk status. Some on Wall Street believe that S&P deliberately stalled. But "a lot of our reason for waiting was weather-related," insists Gerald Hirschberg, an S&P corporate-ratings director. He adds, "I think they did" dodge a bullet.

SAVED: *No Chapter 11 yet*

Kmart says it doesn't feel grazed. Robert Burton, director of investor relations, says an earlier downgrade wouldn't necessarily have meant bankruptcy. Still, he concedes, the threat of a junk rating hung over the talks.

With Kmart bonds trading at junk levels since fall, Wall Street was anticipating junk status. That's why some on the Street are skeptical. "It was all orchestrated," says Wayne Hood, a Prudential Securities analyst. Bondholders won't comment. But bankruptcy still looms if Kmart doesn't boost its numbers this spring. "They have one more shot," Hood says. This is one that Kmart can't afford to miss. *Keith Naughton*

FAT-CAT FOLLIES

TELECOM: HOW THE PORK GOT PULLED

SENATOR HOWELL HEFLIN (D-Ala.) was set to carve out a juicy piece of pork for the rural cable companies in his state, but instead he's encountering static. Heflin tried to slip a provision into the telecom reform legislation to exempt markets where cable operators have fewer than 20,000 subscribers from a rule that would bar local phone companies from buying cable systems. That would have opened the door for local phone companies, big and small, to go on buying sprees and drive up the valuations on small cable systems.

HEFLIN: *Static on the line*

Then a group representing small phone companies got on the line. It liked Heflin's proposal but didn't want to get into a bidding war with the Baby Bells and their ilk to win those cable jewels. So, helped by Representatives Vic Fazio (D-Calif.) and. Charles Norwood Jr. (R-Ga.), rural phone lobbyists altered the wording so that only phone companies with revenues under $100 million could bid. Now, Alabama's dominant phone companies, $20 billion GTE and $17 billion BellSouth, the most likely cable buyers, are frozen out. Heflin's office says he is trying to remove the cap. *Mark Lewyn*

THE LIST GO DIGITAL, YOUNG MAN

The future looks bright for Net surfers and computer whiz kids, according to a study conducted by the executive search firm Christian & Timbers. With so many Internet opportunities and so few workers trained in the complex ways of the World Wide Web, chief technology officers and other techies are in high demand for 1996. But continued downsizing has put human resources directors on the not-so-hot list.

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HOT AND NOT-SO-HOT JOBS

HOT	INCREASE IN DEMAND
General manager of Internet-related companies and CEO of technology-related startups	320%
CEO with a customer-focused approach	133
Vice-president of multimedia content	109
Chief technology officer	96
Senior private banking executive	72

NOT SO HOT	DECLINE IN DEMAND
The CEO who puts the bottom line first	15%
Vice-president of diversity	25
Acquisition/spin-off analyst	56
Administrative assistant	57
Human resources executive	68

DATA: CHRISTIAN & TIMBERS INC.

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Readers Report

DIFFERENT TAKES ON TOP MANAGERS

Your article "The top managers of 1995" (Cover Story, Jan. 8) begins: "Good managers know how to cut: They trim costs, reengineer, and restructure. Great managers know how to grow: They realize you can't shrink your way to greatness." You took the words right out of my mouth.

Dwight L. Gertz
Vice-President
Mercer Management Consulting
Lexington, Mass.

I would have gauged the success of my "top 25 managers" by measuring the number of jobs they created in 1995 instead of how many divisions they spun off, how many plants they closed, or how they circumvented antitrust laws to create another megamerger.

When I was a teen, I used to enjoy reading business magazines because they were filled with stories of entrepreneurship and industry leaders who were bringing forth new technologies and new services.

I congratulate the 1995 winners, but I hope the 1996 list of top managers will be composed completely of industrialists who have fostered employee loyalty and grown their companies, without "downsizing."

J. Tyler Ballance
Hampton, Va.

Your story was noteworthy as much for its inattention to people skills as to its focus on dealmaking and financial results. Is an excellent manager simply a person who achieves outstanding results regardless of how he or she treats the people who do the work?

Under this definition, anyone emulating a robber baron would qualify as a top manager.

David Frances
President
EAP Systems
Woburn, Mass.

C. Michael Armstrong at Hughes Electronics got credit as a top 25 manager.

However, the other side of the story is how he beat Hughes employees. Tens of thousands were laid off (despite substantial increases in profits), plants were closed in four locations, severance benefits were cut 50%, corporate 401(k) contributions were reduced, jobs were moved out of the state and country, other jobs were outsourced, and employees were blocked from transferring to other Hughes Group divisions that have jobs. Hughes is also trying to take $1 billion out of the employees' retirement fund.

These are the employees Mr. Armstrong congratulated for their contribution to cold war victory.

John Chevedden
National Organization of Downsized Employees
Redondo Beach, Calif.

It would be an obvious comment for me to say shame on the U.S. that only two females appear in your top 25 managers of 1995. Your magazine probably does not need to revisit its selection criteria, however you can do something about the subliminal messages that continue to skew the male-female ratio of upper management to the country.

Chauvinist Award of the Year must go to BUSINESS WEEK for the biased writing that slated the tiny paragraph on Ana Patricia Botín more to her father than to her. As if that weren't enough, you gave the slant even more visibility by subheading the paragraph "Like father like daughter."

Has Ms. Botín really done so little as her own person? In that case, why is

CORRECTIONS & CLARIFICATIONS

A chart in "They're having a capital time" (Industry Outlook, Jan. 8) contained an incorrect forecast for net new machine tool orders in 1996. BUSINESS WEEK's actual estimate is $5.29 billion.

Business Week

A Division of The McGraw-Hill Companies

JANUARY 29, 1996 (ISSN 0007-7135)*** 3460

Executive, Editorial, Circulation, and Advertising Offices: The McGraw-Hill Companies, Building 1221 Avenue of the Americas, New York, NY 10020. Telephone: 212-512-2000. Telex: Domestic 12-7960 Int'l 2-60125[illegible]. Subscription rate $49.95 per year; 2 years, $79.95; 3 years, $99.95. Single copy $2.75 each. Write for rates to other countries. Postmaster: send address changes to BUSINESS WEEK, P.O. Box 430, Hightstown, NJ 08520. Second-class postage paid at New York, NY, and at additional mailing offices. Publication Mail Agreement No. 246154

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she even on the list of the best 25 managers of 1995? Get conscious!

Meredith Rutter
President
Publicom Inc.
Acton, Mass.

I was surprised to observe the notable omission of IBM's Lou Gerstner in the top 25 list.

Shiv Kumar
HCL America Inc.
Stamford, Conn.

BUSINESS WEEK should at least have given honorable mention to Caterpillar's Donald Fites.

Hanns John Maier
Ubatuba, Brazil

I noted your description of the accomplishments of Alain Prestat of Thomson Multimedia. One of the key selling points of its satellite dish is its size. But the size of the dish is 18 inches, not 12 inches.

Peter Au-Yang
Philadelphia

You should have included Bob Allen, CEO of AT&T, the executive who made not only the smartest but the gutsiest business decision of the year.

Jesse R. Mohorovic
Richmond, Va.

SHORTSIGHTED AT BAUSCH & LOMB?

This letter, regarding your article "Judgment day at Bausch & Lomb" (News: Analysis & Commentary, Dec. 25), concerns Bausch & Lomb outside director William H. Waltrip [who is slated to become interim chairman and CEO]. Mr. Waltrip in previous positions rode Pan Am to its demise, then stepped off with his golden parachute into the CEO's position at Purolator Courier, which he also reduced to a shambles. He now is positioned to continue his mischief at Bausch & Lomb.

Doesn't anyone ever look at past performance before bringing these hired guns into responsible positions? As a stockholder, I advocate making directors more responsible for their actions by paying at least one-half of directors' fees in company stock purchased at market prices, on the day of board meetings, and held in escrow until termination of directorship. Directors work for the shareholders, and they should be ready to answer financially for their decisions.

Charles C. Christiansen
Oak Harbor, Wash.

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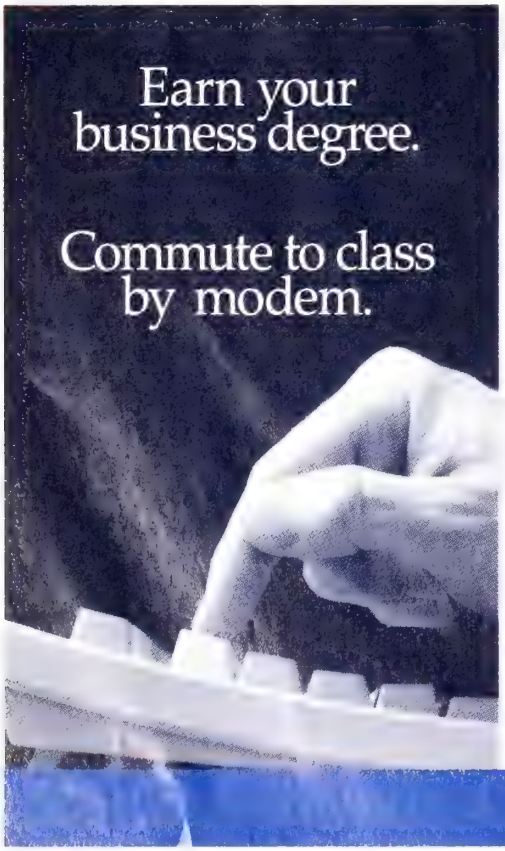

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NIGHTLY BUSINESS REPORT

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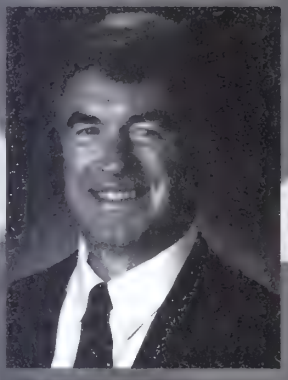
Campbell Soup Company



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TAKEDOWN
The Pursuit and Capture of Kevin Mitnick, America's Most Wanted Computer Outlaw—by the Man Who Did It
By Tsutomu Shimomura with John Markoff
Hyperion • 324pp • $24.95

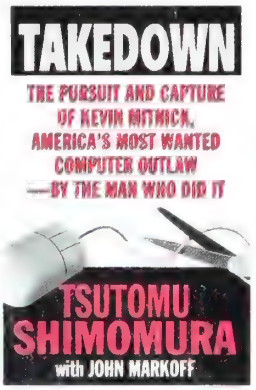
THE FUGITIVE GAME
Online with Kevin Mitnick
By Jonathan Littman
Little, Brown • 383pp • $23.95

MANHUNT ON THE INFO HIGHWAY

Why does the world need two well-written, fast-moving books about the same course of events—the pursuit and capture a year ago of America's most-wanted computer hacker? Because these accounts actually complement each other. Jonathan Littman's *The Fugitive Game* and *Takedown*, by Tsutomu Shimomura with John Markoff, might have overlapped to the point of overkill. Instead, each fleshes out the other, making them well worth reading in tandem.

The focus of both books is Kevin Mitnick, a thirtysomething technical wizard with a reputation for being the most dangerous and unrepentant hacker in cyberspace. More than a decade of often overheated press accounts have made Mitnick's hacking skills legendary—whether used to crack a central-office telephone switch, scam free cellular-phone calls, or, most notoriously, getting into almost any computer on the Internet.

For the most part, Mitnick used those skills to pull relatively harmless and sometimes inspired pranks, such as inflating an enemy's phone bill by $30,000. Arguably more serious was his nabbing the source code for Digital Equipment Corp.'s VMS operating system. Through it all, though, his main gift seems to have been what hackers call social engineering—talking his way into a telephone company office, say, to obtain computer passwords and other secrets.



As the events described here began to unfold in early 1994, Mitnick was on the lam, having disappeared while on probation two years before. He had fled the Los Angeles area, where he had grown up, but he was still making himself heard and felt throughout cyberspace, contacting fellow hackers, taunting his pursuers with bogus E-mail, and making late-night calls from a rigged cell phone.

One of those he telephoned frequently was Littman, a journalist who was steeped in the underground computer culture and who, Mitnick had learned by surreptitiously reading Littman's E-mail, was preparing a story about it for *Playboy*. Using his hacker skills to hide his whereabouts and avoid possible wiretaps, Mitnick made dozens of calls to Littman beginning in May, 1994. Mitnick found Littman sympathetic and hoped the writer would help the world better understand him. Mitnick vehemently denied the worst capers attributed to him, such as breaking into U.S. air-defense computers in 1979. Most of all, he sought to erase his FBI-fostered image as an "electronic terrorist" who stole money from computer nets and who might even remotely launch nuclear missiles.

That *Playboy* article might have been all that got written, but, thanks to intervening events, we have two books. On Christmas Day, 1994, Mitnick allegedly broke into a computer run by Shimomura, a computer-security expert at the University of California at San Diego. In less than two months, even as Mitnick continued calling Littman, Shimomura used his own considerable skills to track Mitnick down so that the FBI could arrest him. At that point, Littman and Shimomura each began to write their books. Shimomura chose as his coauthor John Markoff, a reporter for *The New York Times* who had discussed Mitnick with Littman and written extensively about the hacker. The upshot is that the three authors and their two stories became entangled, which is why the books are best read together.

Far from "flaming" Mitnick, Littman goes to considerable pains, including midnight telephone assignations at prearranged phone booths, to determine just what makes the hacker tick. Among his revealing answers: Mitnick isn't motivated by money but by a desire for power—power over machines and, through them, over people.

The final hunt for Mitnick is best described by Shimomura and Markoff who, unlike Littman, were there. Unfortunately, most of the action consists of Shimomura and his antihacker team probing the Internet from their computer screens, eating fast food, and jumping in and out of rental cars—not the most heart-stopping stuff. Still, he and Markoff have done a good job of making many technicalities accessible and conveying a sense of hot pursuit.

Littman tries to have the final say, mainly by questioning his competitors' motives. As other writers have done, he asks whether Markoff violated journalistic ethics by directly helping in the hunt for Mitnick. What's more, Littman accuses the reporter of having used his *Times* stories about Mitnick's capture to hype the hacker's profile and thereby win a larger advance and better movie deal for the book he intended to write with Shimomura. Markoff, in a letter printed in Littman's book, denies both charges.

Littman offers another twist: He speculates that Shimomura may have been a spook secretly employed by a government agency, not just a do-gooder academic. Even if his conjectures are overblown, Littman's is the more adventurous of the books, since it tries to probe beneath the sensationalism surrounding Mitnick and computer hacking.

Inadvertently, perhaps, both books describe an America worthy of Thomas Pynchon. As in that author's *Gravity's Rainbow*, Mitnick and Shimomura live in a world that's chock-full of brand names, rife with technology, flooded with electronic signals, and fraught with paranoia. Shimomura, for instance, never goes Rollerblading without a cell phone in his fanny pack. Beepers constantly interrupt the phone calls of people who are simultaneously staring at computer screens or fax machines. Any E-mail, it seems, may be a prank by Mitnick or a plant by the FBI. If there's one message that comes through loud and clear, it's that cyberspace is a world of mirrors and ever-shifting identities, of which Mitnick is one of the most fascinating.

BY JOHN W. VERITY

Verity is BUSINESS WEEK's information-management editor.

THE BUSINESS WEEK BEST-SELLER LIST

HARDCOVER BUSINESS BOOKS

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14 **THE FIFTH DISCIPLINE** by Peter Senge (Currency • $18.50) *Creating the "learning organization."*

15 **ONE UP ON WALL STREET** by Peter Lynch, with John Rothchild (Penguin • $12.95) *Make money using what you already know, says the former Fidelity fund manager.*

BUSINESS WEEK's Best-Seller List is based on a survey of chain and independent booksellers that carry a broad selection of books on economics, management, sales and marketing, small business, investing, personal finance, and careers. Well over 1,000 retail outlets nationwide are represented. Current rankings are based on a weighted analysis of unit sales in December.

HOT TYPE

"POOH'S TUMMY BEGAN TO RUMBLE. 'DOES solving problems always make you so hungry?'"

Or sleepy? Talk about bedtime stories: *Winnie-the-Pooh on Problem Solving* by consultants Roger E. Allen and Stephen D. Allen (Dutton) made me awfully snoozy. Unfortunately, the book, which weighs in at No. 4 on this month's BUSINESS WEEK Best-Seller List, is intended to wake up readers. A sequel to *Winnie-the-Pooh on Management*, which its publisher says has sold more than 100,000 copies in the U. S., it offers instruction in the authors' approach to getting out of conundrums.

Their five-step SOLVE method will strike most adults as pretty basic: Select a problem, define it carefully, examine all of its aspects, brainstorm about possible solutions, refining one of them—then give that solution a try while monitoring the results. Each step is discussed by Pooh, his friends Piglet and Eeyore, and the know-it-all Stranger in excruciating detail—just in case the reader isn't smarter than the average bear. The all-too-precious dialogue will have even 8-year-olds hankering for a couple of rounds of *Mortal Kombat*.

What's best about *Winnie-the-Pooh on Problem Solving* is that it reproduces illustrations and lengthy bits of text from the original A. A. Milne books. But for that, you could just pick up a copy of *The House at Pooh Corner*. Problems, schmoblems—a trip to the Hundred Acre Wood ought to be worry-free.

BY HARDY GREEN

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BY STEPHEN H. WILDSTROM

PASSING THE SCREEN TEST

Monitors are using more sophisticated technology–and prices are dropping

So you just bought a spiffy new computer system: multimedia capability, high-resolution monitor, the works. Text and graphics look great. But those videos. They're so dark and murky. What a disappointment. You can't do much about it today, but please stand by. Some new technology coming down the Infopike will help a lot.

The technology behind the television-style monitors that we use hasn't improved much since the mid-1980s. But I'm writing this column using an LCD1280 desktop display from NEC Technologies (800 632-4636). Although the screen measures just 13 inches from corner to corner, the display's extremely high resolution—1,280 by 1,024 pixels—lets it show as much information as a conventional 20-in. monitor. And while cramming more into a smaller area causes text and images to shrink, you can comfortably sit much closer to an LCD screen than to a TV-type monitor.

CLOSING THE GAP. The LCD1280 was introduced last year with a staggering $11,750 price tag. But this month, NEC is coming out with a new 13-in. version at $6,000 and a 12-in. model at $4,000. Such prices are still way too high for these units to grace many desktops—a top-of-the-line 20-in. monitor costs around $2,000. But flat-panel screen prices are expected to continue to plunge, and desktop units cheap enough for real-world budgets may not be that far away.

Just look at what's happening in laptops. A year ago, a 10.4-in. active-matrix was found only on $5,000-plus notebooks. Now they're turning up on laptops in the $2,500 class, such as the IBM ThinkPad 365C. The price differential between active-matrix and the older, less vivid passive-matrix screens is down to about $500. At the top end, several manufacturers are offering laptops with 12-in. displays. Because the full area of a flat panel is viewable, while a considerable part of a cathode-ray tube screen is lost within its case, a 12-in. laptop screen has nearly the same viewing area as a 14-in. monitor. Flat-panel makers, such as Sharp and Hitachi, are ready to make bigger displays, but that would require a bigger laptop case.

The trusty CRT monitor is also due for an overhaul. Current monitors are designed to make text on the screen as crisp and readable as possible, hence the poor appearance of videos and other images. Later this year, NEC will introduce new monitors that use a technology different from either of the two borrowed-from-TV systems used by current CRTs.

STRONG PALETTE. Prototype units that I have seen give much livelier video images without sacrificing text quality. No pricing has been announced, but the new displays will likely be competitive with current high-quality models.

Two other display techniques may also make an impact soon. New plasma technology being developed by Sony, Fujitsu, and others could be used to build flat-panel screens as large as 50 in. Sony demonstrated a 24-in.-by-15-in., 3.75-pound prototype Plasmatron at last fall's Comdex trade show. While blues are a little weak, other colors are lively, and the images are very sharp. For even bigger displays, Texas Instruments' Digital Micromirror Device (DMD) technology could produce much brighter projection systems for presentations or home theaters. The first product to incorporate the device, the $9,500 Diamond D-400 from nView (800 736-8439), claims to project a viewable computer image in normal room lighting.

Consumer devices that employ either the Plasmatron or the DMD technology are at least a couple of years away. But you can bet there's a bigger, brighter—and maybe even cheaper—display in your future.

VIVID: *One of NEC's new LCD monitors*

BULLETIN BOARD

BOOKS

CD-ROMs DEMYSTIFIED

Some of the many frustrated computer owners who sent me tales of woe in response to "Wanted: A PC for the masses" (Jan. 15) may find some relief in *Make Your CD-ROM Work!* by Bob LeVitus and Ed Tittel

(Random House, $10.95). The book offers advice on what to do about that all-too-common experience: popping a new multimedia disk in your CD-ROM drive and having nothing come out but a stream of error messages. Topics include sound cards, video adapters, and memory settings. About two-thirds of the breezy, question-and-answer text is devoted to Windows and DOS problems, the rest to the less trouble-prone Macintosh.

INTERNET

SPANISH SPOKEN HERE

Reader Ken Leebow of Marietta, Ga., has found a novel use for VocalTec's Internet Phone ("It's for you—on the PC," Jan. 8), one of several products that make it possible to hold voice conversations over the Internet. His 13-year-old son, Josh, uses it to practice his Spanish. He looks for fellow Internet Phone users in South America, then strikes up conversations with them on the Net. "He used to hate Spanish," Leebow reports. "Now he has fun while learning."

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BY ROBERT KUTTNER

SOCIAL SECURITY: LET'S NOT TRADE IT IN FOR A LEMON

FLAWS

Yes, the system will need shoring up soon. But privatizing it, à la Chile, could turn out to be a remedy worse than the disease

Robert Kuttner is co-editor of *The American Prospect* and author of *The End of Laissez-Faire*

Once the debate on balancing the budget finally ends, America faces another great fiscal issue: how to stabilize Social Security. The hysteria about looming bankruptcy is exaggerated, but even defenders of the present system admit that Social Security is not in long-term balance. Early in the next century, we will need to raise the retirement age, pare benefits, or raise taxes. This is simply the result of shifting demographics—people living longer and a declining ratio of workers to retirees.

A more radical change would divert some of the income stream from the payroll tax to create privatized annuities. To make up the loss, Social Security pensions would be more heavily taxed or capped. Senators Bob Kerrey (D-Neb.) and Alan K. Simpson (R-Wyo.), for example, would take two percentage points of the current payroll tax to create super individual retirement accounts.

A more sweeping revision is being promoted by Sam Beard, author of a forthcoming book titled *100 Million Millionaires*. Beard's idea is to use four percentage points of the Social Security tax to finance private retirement accounts. The proceeds would underwrite retirement and could be passed along to heirs. He calculates that after 45 years, every individual with $10,000 or more annual income would accumulate at least $1 million in savings (or $182,000 in today's dollars). Eventually, thanks to compounding, a fully funded retirement system would replace the present one and create a society of secure rentiers.

PINOCHET'S CRAPSHOOT. There are problems with this scheme, however. Obviously, it diverts money from the Social Security system earmarked to finance pensions for current and future retirees. Beard proposes to make up that shortfall by raising the retirement age to 70, reducing the inflation adjustment of Social Security pensions, and increasing federal borrowing during the 30- to 40-year period in which the new system matures.

Beard's proposed system is also highly redistributive (just as the current Social Security program is), since it uses the taxes paid by more affluent workers partially to subsidize the retirement accounts of less affluent ones. The risk is that Beard's proposal would become a stalking horse for the dismantling of Social Security as a universal system.

Enthusiasts of this approach often invoke the experience of Chile, where the August Pinochet regime and its University of Chica go-trained economist-advisers privatized th public retirement system. Today, Chilea workers pay taxes into one of several pri vate retirement plans. Supposedly, the goverr ment will make up the difference if retiremer benefits do not equal at least 75% of the sub sistence level. The funds are currently doin well, but genius is a rising market. One o more of the funds could tank. Stocks fall a well as rise—remember the U.S. in th 1970s? When the first retiree begins claimin benefits in 2005, the "privatized" Chilean sys tem could face a public bailout crisis—or sim ply shortchange retirees.

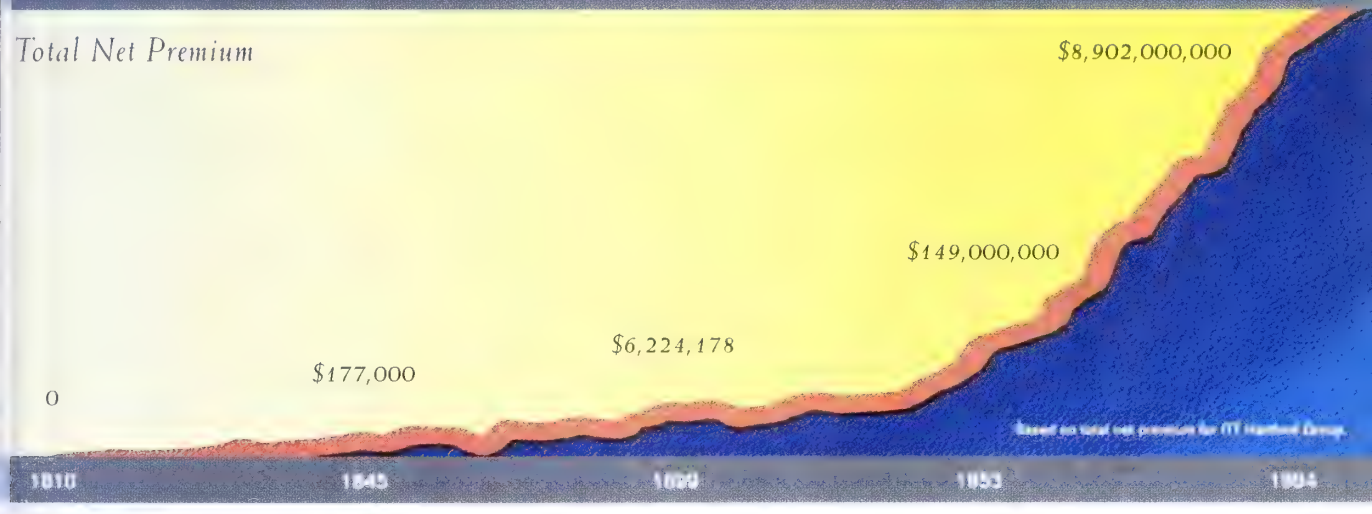
Still, there is the germ of an importan idea here. The current Social Security systen is almost pure income transfer. Taxes from to day's workers pay the pensions of today's re tirees. Unlike a funded pension plan or annu ity, most of the payouts are not a return o capital. The current capital surplus in the So cial Security system generates income that fi nances a small fraction of total payouts.

PIES IN THE SKY. Turning Social Security into a funded pool of capital would raise the nation al savings rate and restore the system to sol vency. However, this approach poses highly charged policy choices. Do we retain a collec tive system or do we splinter it into individu al accounts? And if money is to be diverte from current payroll taxes, who makes up the loss?

In principle, there is a left-right grand bar gain to be had. The left gets Social Security solvency but allows partial privatization. The right concedes the need for a universal, state mandated system but gains one with private ly invested capital.

Beard's plan is reminiscent of populis schemes for spreading the wealth, most o which in practice were captured by the usua suspects: The populist crusade of the 1890s fo an elastic currency turned into the safely con servative Federal Reserve System. Louis O Kelso's plan to turn every worker into a cap italist spawned Louisiana Senator Russell B Long's employee stock ownership plans—most of which are used by ordinary corporations as a cheap way of raising capital. The one share the-wealth scheme that actually worked as advertised is none other than... Social Se curity. Before we cash it in, we should be sure what we are getting in return.

WHEN you SPEND as MUCH TIME WORRYING about your POLICYHOLDERS as your SHAREHOLDERS, an INTERESTING THING HAPPENS.



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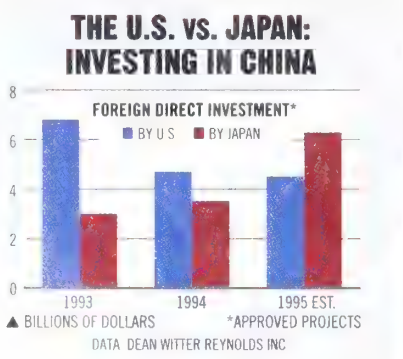
BY GENE KORETZ

A MARRIAGE MADE IN ASIA

Sino-Japanese ties worry the U. S.

In its dealings with Japan and China, the U. S. would do well to keep a weather eye on the fast-growing economic alliance being forged by the two Asian nations. For one thing, Japan's direct investment in China has begun to take off, jumping by 78% last year and outstripping U. S. investments by 40% (chart). Indeed, economist Chen Zhao of *The China Analyst*, a publication of the Bank Credit Analyst Group in Montreal, reports that Japanese companies now regard China as their main investment target and plan to place half of their overseas capacity increases there.

Moreover, Joseph P. Quinlan of Dean Witter Reynolds Inc. estimates that Sino-Japanese trade flows exceeded U. S.-Chinese trade last year for the first time since the 1980s. At the same time, with U. S. exports to China running only about one-third the size of China-bound Japanese exports, America's $38 billion trade deficit with China dwarfed Japan's $12 billion shortfall.



Looking ahead, Chen observes that Japan's China policies may well give it a leg up vis-á-vis the U. S. in building trade relations. It rarely has mixed business with politics, for example, and since 1979, it has provided China with over $33 billion in government loans, export credits, and other forms of financial aid, compared with a paltry $300 million in export credits extended by the U. S.

Japan also is more sympathetic to China's slow-paced economic reforms and its desire to maintain a strong government role in economic policy. By contrast, the U. S. has pushed rapid liberalization and market-oriented reforms, as well as human-rights issues.

Ironically, says Quinlan, Japan's growing investment in China may well exacerbate U. S. trade frictions with the Chinese. That's because many Japanese products that were once exported from Japan are now being assembled and shipped from China, widening America's huge trade deficit with that nation.

RUMOR MILLS BOOST M&A BILLS

A study finds secrecy cost-effective

Loose lips can cost merger-minded companies big bucks. That's the conclusion of a new study of stock movements associated with mergers and acquisitions by G. William Schwert of the University of Rochester.

Schwert looked at pre-bid and post-bid rises in share prices of some 1,400 companies acquired in takeovers from 1975 through 1991. Since he found that the size of pre-bid runups had no effect on stock price rises occurring after bids were announced, he concluded that the early runups added to acquisition costs. Otherwise, anticipatory price gains would have subtracted from post-announcement stock increases.

As it is, Schwert found that shares of targeted companies appreciated about 30% from a period starting two months before the first bid and ending with the deal's consummation—with the price action evenly divided between the pre-bid and post-bid periods. The clear lesson for companies planning acquisitions, he says, is that they are likely to save themselves and their shareholders a bundle if they can keep the pending move under strict wraps.

DANGERS OF BUDGET BRAWLS

Will a stalemate lead to recession?

Since the recent failure of Congress and the President to reach a balanced-budget accord caused interest rates to surge, you might think a protracted budget stalemate would produce more of the same. Not so, says Paul A. McCulley of UBS Securities Inc.

Without a deal, notes McCulley, Congress is likely to continue funding the government under continuing resolutions rather than normal appropriations bills. But continuing resolutions usually require spending to stay below year-earlier levels, while appropriations bills incorporate "normal" increases to reflect inflation. And that means fiscal policy would be even tighter than it would be if a balanced-budget deal were passed.

The upshot, says McCulley, is that going the continuing-resolution route could increase fiscal restraint "enough to tilt the economy close to the recessionary precipice—and strongly reinforce the case for Fed easing."

THE NEW MATH OF POLITICS

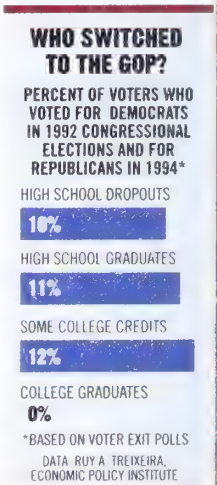
Voters want more than rising GDP

By all odds, relatively healthy U. S. economic growth in 1993 and 1994 should have enabled the Democrats to retain control of Congress in 1994—even though the party in power usually loses some ground in midterm elections. The reason they didn't, writes Ruy A. Teixeira of the Economic Policy Institute in the current issue of *Challenge*, is that the expansion failed to improve the lots of average Americans.

Teixeira's analysis of exit poll data indicates that it was non-college-graduate voters, particularly whites, who deserted the Democrats in droves. Among white men with only high school diplomas or just some college learning, for example, Democratic congressional support dropped by 20 and 15 percentage points, respectively, from the preceding 1992 elections.

It's exactly these groups whose wages have fallen in recent decades—and continue to languish. Teixeira notes that median real hourly earnings for full-time male and female workers fell 3.3% and 1.7% from 1992 to 1994. Some 36% of voters who felt their economic situations had worsened said they shifted from Democrat to Republican in 1994.

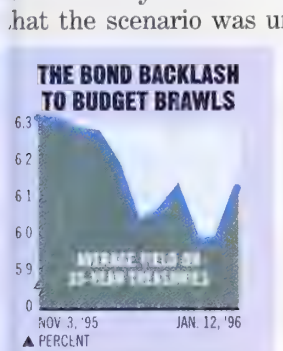
The Republicans successfully wooed such voters with promises that cutting government spending, welfare, and taxes will cure their economic woes. The Democrats' challenge is to offer a compelling countervision.



BY JAMES C. COOPER & KATHLEEN MADIGAN

FIDDLING IN WASHINGTON COULD BURN THE ECONOMY

U.S. ECONOMY A couple of months ago, forecasting the economy in 1996 looked like a no-brainer. Growth was slowing as businesses adjusted their inventories to the cooler pace of demand, but the economy was set for a lift from lower interest rates as soon as Washington could cobble together a plan to cut the deficit. Last quarter's bond market rally and Federal Reserve easing suggested that the scenario was unfolding right on cue.



That was then. Now, the question is no longer when Washington will hammer out a budget deal, but whether there will be one at all. The answer will affect both Wall Street and this year's outlook. Take away a credible budget package, and you yank a key prop from under the economy.

The promise of a historic step toward fiscal responsibility sent the benchmark yield on the 30-year Treasury bond to below 6% in December for the first time in more than two years. Many analysts believe that yields can sink to 5.5% or lower, with attendant benefits for mortgage refinancing, consumer debt burdens, housing, and a broad array of durable goods.

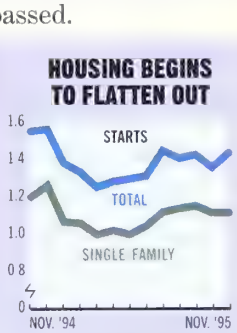
BUT IN A MATTER OF DAYS in early January, bond yields jumped from a low of 5.95% to as high as 6.20% as the talks hit a roadblock (chart). The power of the budget debate to sway the market was evident once again on Jan. 16. News that the two sides would simply meet again coincided with investor George Soros' comments that sent the dollar higher. The combination pushed yields from 6.14% to 6.05% in a single day.

Even so, yields remain higher than economic fundamentals would dictate. The danger is that long-term rates could go even higher with another round of disappointment over Washington's intransigence and worries about the reckless attitude of many in Congress toward the debt limit and a possible default.

House Budget Chairman John R. Kasich (R-Ohio) attempted to allay those worries on Jan. 14 by expressing confidence that the debt ceiling will be raised. But afterward, Representative Nick Smith (R-Mich.), head of the 160-member House Debt Limit Coalition, called the debt limit a "reasonable tool" in the negotiations. Wall Street bristles at such naiveté, understanding that the default issue is financial-market gunpowder that could also blow the economy out of the water.

If cooler heads remove the debt-limit issue, the worst-case budget scenario is "no deal" and a continuing resolution for the rest of fiscal year 1996. Such a situation would keep bond yields higher than they would have been with a deal. But the damage would not be great, in part because the market knows the Republicans would still control the discretionary spending in the appropriation bills not yet passed.

Washington's bickering also offsets world economic conditions that would otherwise be especially favorable for lower U.S. bond yields. The dollar has strengthened. Europe is cutting rates in the face of an economic slowdown, as Germany and France flirt with outright recession. And Japan's recovery will be slow.



Global weakness may hamper what has been a sharp improvement in the U.S. trade deficit. The trade gap narrowed to $8.04 billion in October, from $8.25 billion in September. Although both exports and imports dipped in October, exports are up 11.3% from a year ago vs. a 7.1% yearly pace for imports.

As for short-term rates, because the government shutdown has held up key economic data by a month or more, the Fed may feel compelled to put off another rate cut until a clearer reading on the economy is possible. Such a delay would come at a time when the economy is slowing but no one knows by how much.

The most up-to-date information the Fed has right now is anecdotal reporting from its 12 districts, summarized in the Jan. 17 Beige Book prepared for the policy meeting on Jan. 30-31. The report said the economy "was growing at a generally modest pace at the end of 1995." Prices were "remaining stable," although "some areas still report shortages of skilled workers," a sign that the Fed is closely watching wage growth.

A MORE DETAILED PICTURE of the economy heading into the new year should begin to take shape now that the Commerce and Labor Depts. are starting to catch up with their backlog of delayed economic reports.

The availability of data means that the ever-fickle bond market may switch its attention away from the budget battle and back to the economy's health. If further data confirm the economy's softness, that would

ERIC HOFFMANN/BW

soothe the markets' disappointment over the budget, taking some upward pressure off yields.

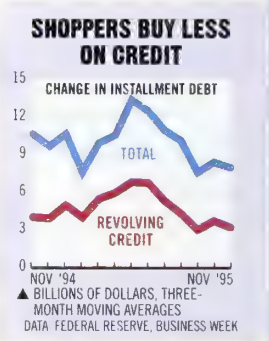
In particular, housing has flattened out, especially in the single-family sector (chart, page 21). Housing starts increased by a larger-than-expected 5.7% in November, to an annual rate of 1.42 million, but all of the strength was in the multi-unit sector, which surged 35.6%. Single-family starts were unchanged at 1.1 million.

Like housing, mortgage applications to buy a home had also flattened out in the final months of 1995, although the level of applications was relatively high. That changed in January—after long rates launched their first budget-related spike. Applications in the first week of 1996 plunged to their lowest level since August. Many would-be home buyers may be waiting for mortgage rates to slip closer to 7% again. But without a budget package, that may not happen.

IN ADDITION, the blizzard knocked housing as well as retail sales onto the mat. That means both industries began the first quarter way below their fourth-quarter averages, so these sectors will have to crawl out of deep holes in order to post any kind of growth.

According to the reports by Mitsubishi Bank/Schroder Wertheim and the Johnson Redbook Service, retail sales fell in the week ended Jan. 13, as the blizzard forced stores to close. Even without two feet of snow, though, consumers would likely be tempering their buying this winter in response to job worries and the need to pay off heavy debts.

Shoppers already were borrowing less in the fourth quarter. Installment credit rose $8.6 billion in November after an $11.2 billion gain in October, said the Fed. Additions to installment credit have been smaller in the second half of 1995 than in the first (chart).



In particular, consumers have scaled down their use of revolving debt, which includes credit cards. Even with the borrowing slowdown, smaller job and income gains suggest that the delinquency rate on credit-card bills edged higher in the fourth quarter, after the third-quarter rate hit the second-highest level in 10 years.

Lower rates would offer relief to some financially strapped households. By switching to credit cards with lower finance charges and refinancing mortgages, consumers would free up extra cash and keep the expansion going forward.

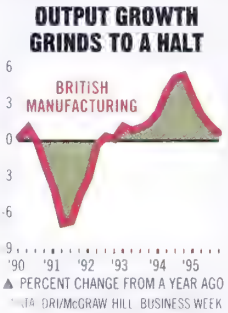
That, at least, is how 1996 is supposed to play out: a budget deal, lower rates, mortgage refis, and continued growth. But as the Washington standoff and the bond market's response show, the best-laid plans of mice and forecasters could easily go astray.

BRITAIN

SLOW GROWTH IS BETTER THAN NONE

The "British model" is facing a test. With Germany and France near recession, can Britain keep the Continent's mess from washing up on its shores?

The answer is yes. Although Britain is slowing down, growth should remain in the plus column, and the seeds for a second-half pickup already are sown. The key reason: A decade of economic restructuring, including privatizations, reduced social costs, deregulated labor markets, and a domestic policy focus, has molded a less inflation-prone economy. That gives the monetary authorities more flexibility to manage growth.



Interest-sensitive sectors will lift demand as the Treasury cuts interest rates further amid political pressure to deliver a solid rebound ahead of elections. Already, firmer home prices, mortgage activity, and fourth-quarter car sales, along with surveys pointing to solid December retail activity, suggest healthier consumer spending. Despite the overall restrictiveness of the new budget, consumers will be better off this year in the face of lower taxes and interest rates—just the opposite of 1995.

The problem is that demand is being sated by excess inventories. Manufacturing output stagnated in November, and December surveys show fading orders and production plans (chart). Construction is also weak, and the slowdown on the Continent is hitting exports.

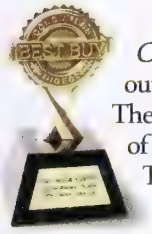
But the restructuring has made prices and wages more flexible, and the weaker economy is reducing inflationary pressures. December output prices for core items slowed and should continue to do so. The underlying rate of retail inflation has been below 4% for the longest period in more than half a century.

Bank of England Governor Eddie George now believes that the government's 2.5% target for underlying inflation will be met in the next 18 to 24 months, a position close to that of Chancellor of the Exchequer Kenneth Clarke. That sets the stage for more rate cuts. Base rates should fall from 6½% now to 6% or less by summer, assuring a second-half rebound.

Another expert tells you where to put your money.

"The Lincoln Town Car is a Best Buy."

Consumers Digest



Consumers Digest calls a Best Buy "a product that offers outstanding value for its price." We call it Lincoln Town Car. The editors were impressed that "this big Lincoln retains the best of what has always been good about large American sedans." The experts agree; even when money is no object, value is.

Three Ways To Lease

$499/$1,999
per month down
24-Month Red Carpet Lease
First Month's Payment*.....$499
Down Payment (Net of RCL Cash)..$1,999
Refundable Security Deposit.....$500
Cash Due At Signing**.....$2,998
30,000-Mile Lease

or

$589/$0
per month down
24-Month Red Carpet Lease
First Month's Payment*.....$589
Down Payment (Net of RCL Cash).....$0
Refundable Security Deposit.....$600
Cash Due At Signing**.....$1,189
30,000-Mile Lease

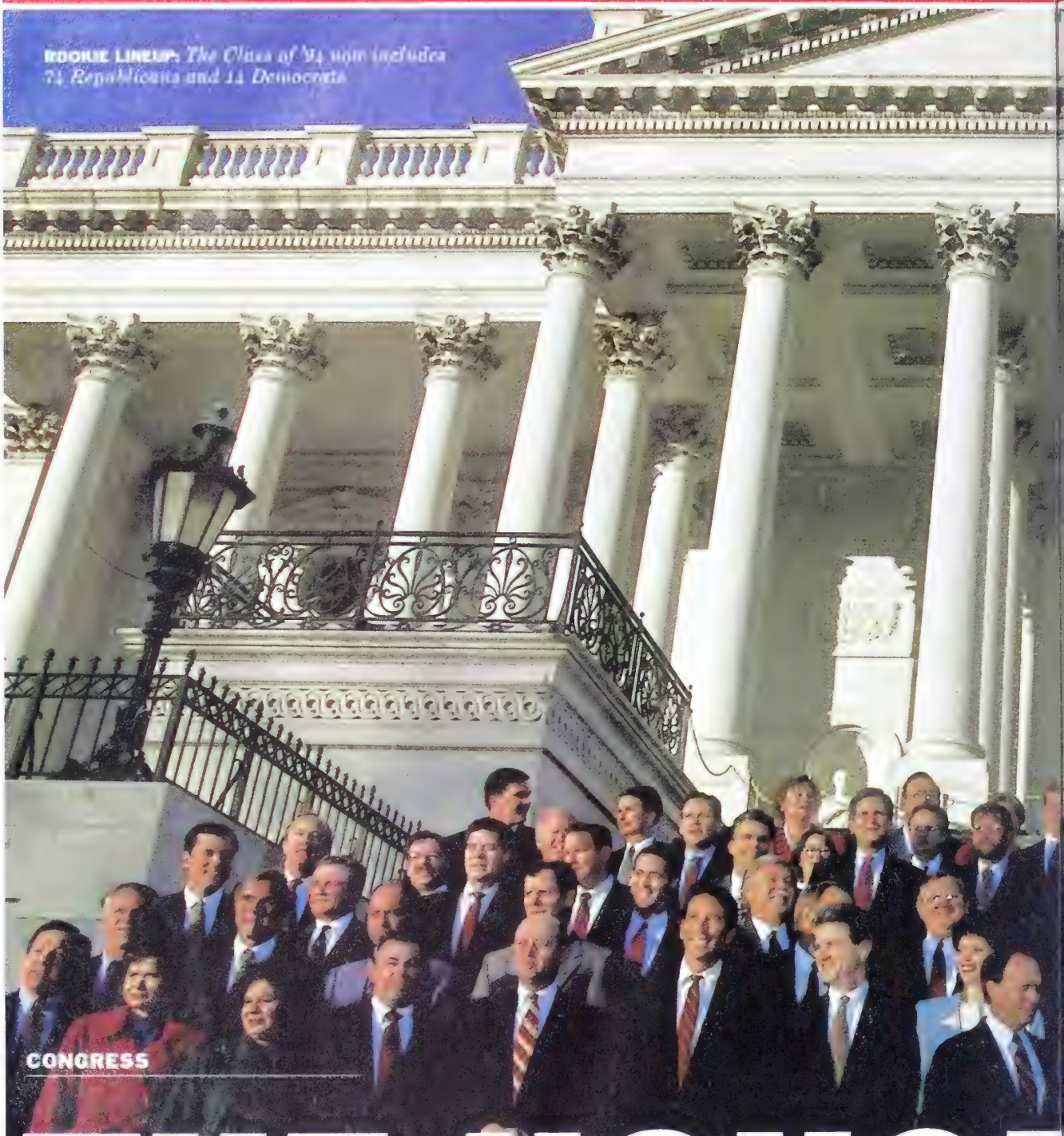
or

$12,584
One-Time Lease Payment
APP Payment (Net of RCL Cash)*..$12,584
Refundable Security Deposit.....$525
Cash Due At Signing**.....$13,109
Cash Outlay Over 24 Months**$12,584
30,000-Mile Lease

LINCOLN
What A Luxury Car Should Be

*'96 Lincoln Town Car Executive Series MSRP $37,550 excluding title, taxes and license fee. Conventional and Advance Payment Program lease payments based on average capitalized cost of 91.0% of MSRP for 24-month closed-end Ford Credit Red Carpet Leases (RCL) purchased in the nation through 11/30/95. Some payments higher, some lower. See dealer for payment/terms. Lessee may have option to buy vehicle at lease end at price negotiated with dealer at signing. Lessee responsible for excess wear and tear and mileage over 30,000 at $.11/mile. Credit approval/insurability determined by Ford Credit. For special lease terms and $3,000 RCL cash, take new retail delivery from dealer stock by 4/2/96. Monthly payments total $11,976 with $1,999 down payment or $14,136 with $0 down payment. Current Lincoln lessees qualify for an additional $500 lease renewal incentive toward a '96 Town Car RCL prior to 4/2/96. See dealer for complete details. **Excludes tax, title and license fee.

ROOKIE LINEUP: *The Class of '94 will include 74 Republicans and 11 Democrats*



CONGRESS

THE HOUSE

GOP newcomers are determined to reshape governmer

FRESHMEN

e they building a new America–or tearing it apart?

For weeks, Republicans pursuing a balanced-budget deal with President Clinton had taken a pummeling in the polls over their scorched-earth campaign to shutter the federal government. But as House Speaker Newt Gingrich left a White House negotiating session on Dec. 19, he saw cause for optimism. With key differences narrowing, Clinton and GOP leaders had agreed to reopen the padlocked agencies. Budgetary peace seemed at hand.

Not for long. Soon after he returned to Capitol Hill, Gingrich ran into the buzz saw known as the House Republican freshman class. The feisty first-termers forced him to scuttle plans to unlock the government, and they demanded that House Majority Leader Richard K. Armey (R-Tex.)—considered more ideologically pure than Gingrich—accompany the Speaker to future talks. "We needed someone who was going to hold the line," says Representative Sue Myrick (R-N.C.), a freshman member of the House GOP leadership.

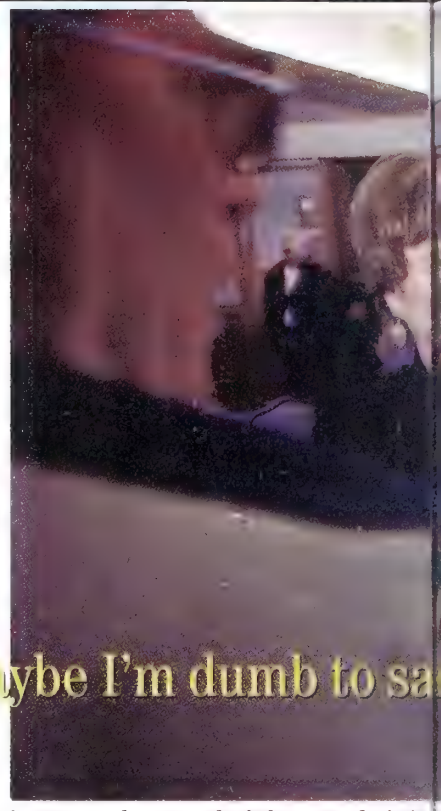
Gingrich's about-face is but one example of the extraordinary influence wielded by the 74 GOP freshmen. By virtue of their size, cohesion, and insistence on a literal enactment of the Contract With America, the first-termers are shaking Washington to its core.

Already, they have pushed policy sharply rightward, in the process raising partisan combat to new heights. They have muscled political reforms past their own skeptical leaders. They prodded Clinton to accept a seven-year balanced-budget timetable based on strict Congressional Budget Office economic projections. And they have surprised even their business backers with a die-hard defense of their conservative principles in a town more comfortable with pragmatic dealmaking. "I wish we had 30 more of them, in both houses of Congress," says Carol L. Ball, CEO of Ball Publishing in Greenville, Ohio. "Then maybe we could get something done."

STEADY COURSE. In an institution accustomed to freshmen who were seen but rarely heard, this new crop has demonstrated unprecedented clout. Clearly, the fervor of the freshmen is the driving force behind the bold Republican plans for remaking government. Yet the man-the-barricades approach of the first-termers—a penchant for confrontation over compromise—has prevented them from implementing most of their vaunted Contract. Indeed, a public backlash against their hardball tactics threatens to stall their revolution just as they are on the threshold of success with their paramount priority: balancing the federal budget by 2002. A BUSINESS WEEK/Harris Poll of 755 adults conducted Jan. 5–8 found that only 26% of Americans approved of the freshman Republicans' tactics, while 70% disapproved (page 28).

Public perception be damned. So far, the freshmen show no signs of changing course. Many are intent on a hardline legislative agenda for '96—including abortion restrictions, an assault on environmental rules, dismantling the federal social safety net, and a repeal of 1993 assault-weapons curbs. The strategic risk: that the first-termers could alienate centrist swing voters and lose control of the House after a two-year reign. "'My way or no way,' could bring a premature end to the Republican majority," says Brookings Institution congressional scholar Thomas E. Mann.

"Maybe I'm crazy, maybe I'm dumb to sa



Even some of the corporate chieftains who cheered the Republican takeover of Congress a year ago haven't lost their enthusiasm. "I'm disturbed because I think they've carried ideology too far," says H. Brian Thompson, CEO of LCI International Inc., a McLean (Va.)-based long-distance telephone company. "Not that the ideology is wrong—but you don't have to do it in one bite." Other executives chide the freshmen for gleefully throwing sand in the gears of government to achieve their budget priorities. "They need to change their rhetoric," says Andrew P. Daly, CEO of Vail Associates Inc., which operates the venerable Colorado ski resort. "I'm ill at ease when you hold government hostage."

Democrats are betting such discomfort will help them recapture the House

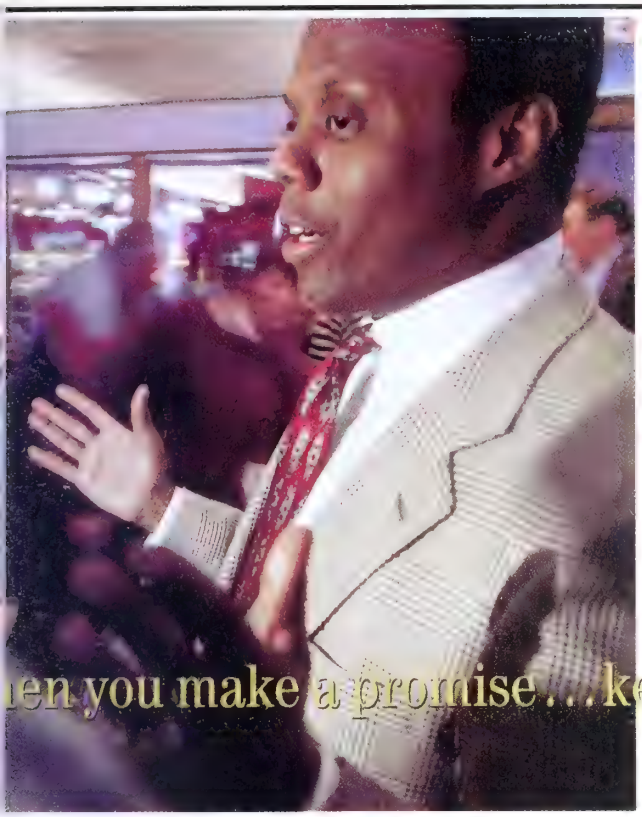
GRADING THE FRESHMEN

BALANCING THE BUDGET Go to the head of the class for forcing President Clinton to move toward a blueprint for erasing the deficit by 2002. But shutting down the government as a negotiating tactic has been a political disaster. **B-**

OVERHAULING CONGRESS AND CAMPAIGN FINANCE Kudos for cutting Capitol Hill staff, streamlining committees, and restricting lobbyists' gifts. But demerits for failing to curb special-interest financing of campaigns. **D+**

REFORMING WELFARE Delivering on promises to overhaul the welfare system is a major accomplishment. A compromise on welfare reform seems in the cards despite President Clinton's Jan. 10 veto of the first attempt. **A-**

GETTING GOVERNMENT OFF BUSINESS' BACK Promises, promises. Vows to stimulate growth through tax cuts and regulatory relief for Corporate America have been stymied by moderate Republicans and conservative Democrats, who see the environmental and worker-safety reforms as too extreme. **C+**



STANDING FIRM: *Oklahoma's Watts meets with voters*

they lost in 1994 after four decades of dominance. "We owe them a great deal," quips Representative Barney Frank (D-Mass.). "Their views are unpopular. And their methods are inept." House Minority Leader Richard A. Gephardt (D-Mo.) describes the new class as "terrorists" with an "insane" agenda. Former House Ways & Means Committee Chairman Sam M. Gibbons (D-Fla.), a 33-year House veteran, dismisses them as "wild and reckless" legislators lacking empathy for the downtrodden. And Clinton is expected to play on public fears of GOP stridency in his Jan. 23 State of the Union address.

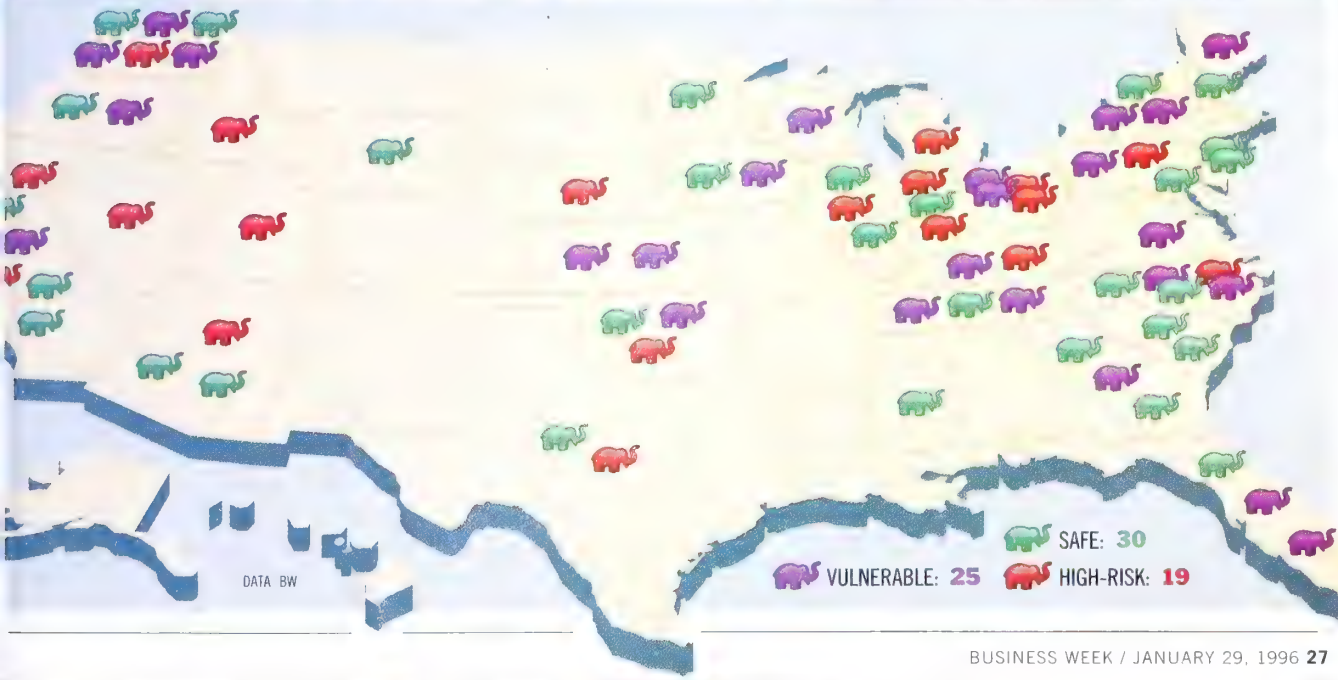
The newcomers contend that their achievements will become evident only over the long haul. "The tough work of freedom is going to take time," says Representative Zach Wamp (R-Tenn.). "We're dealing with a very sick patient, and you can't wake him up in the middle of surgery and ask how he's doing." Moreover, the freshmen believe voters endorsed their tough tactics by electing them on the vow to enact the Contract. "We know why we were sent here, and we will act regardless of the consequences," insists Representative David Funderburk (R-N.C.). "If there is a price, so be it. There'll never be another opportunity like this in our lifetime."

Maybe so. But the unwillingness of the new class to compromise with the White House and Senate moderates has limited its accomplishments. Aside from some congressional reforms, such as reducing staff and eliminating some committees, the freshmen have yet to deliver a balanced budget, tax cuts, regulatory relief, term limits, and litigation reform. Concedes Representative Phil English (R-Pa.): "We have to do more before we declare victory."

"LIKE TEENAGERS." As the largest freshman class since the Democratic "Watergate Babies" of 1974 (page 32) prepares to face the voters this fall, its legacy remains unclear. "The freshmen are the testosterone of the House Republicans," says Claremont McKenna College political scientist John J. Pitney Jr. "Testosterone adds muscle mass, but in excess it can lead to overaggressiveness and health problems."

Judging by early polls, some freshmen could suffer terminal side effects from their pugnacity. Although the BUSINESS WEEK/Harris Poll found that 49% of Americans see the first-termers as "a new breed of politicians," 45% consider them "extremists." That view is reflected at the grass roots. "They're acting like teenagers, and I'm just sick of it," says Chad Bosworth, 20, a junior at Indiana's Ball State University. "It's high time for these young whippersnappers to wipe their noses and get down to business," scoffs Polly Elkins,

FRESHMAN GEOGRAPHY



president of the Cherokee Democratic Women's Club in Chattanooga, Tenn.

Other Americans are willing to give the first-termers more time to mature. "The freshmen represent the views that are going to turn this country around," says Ted H. Smith, an Oklahoma City stockbroker with Dean Witter Reynolds Inc. "They're doing what they had said they would do." Jeffrey T. Grade, chairman of Harnischfeger Industries Inc., a Milwaukee heavy-machinery maker, feels that the freshmen "are acting like the rest of America—tired of business as usual. They are inexperienced and unskilled, but maybe that's what we need."

One key booster: Texas tycoon Ross Perot, who finds a natural kinship with their maverick ways. The GOP tyros have "a deep commitment to putting our country's house back in order," Perot says. "Most have shown great courage and tenacity in working to get the job done right."

Any way you look at it, the new class represents a sharp departure from its predecessors. In a chamber dominated by lawyers, most of the newcomers have been small-business owners or corporate executives. They speak the language of commerce and are evangelistic about the desire to slash taxes, regulations, and paperwork. "We're not extremists," says Michael P. Forbes (R-N.Y.) "We were meeting payrolls, paying bills, and getting fed up with Washington. And we decided to do something about it."

Few of the freshmen are government careerists—only 27 have previous legislative experience. Several are celebrities, including former pop singer Sonny Bono (R-Calif.) and football stars Steve Largent (R-Okla.) and J.C. Watts Jr. (R-Okla.).

CONTRACT WORKERS. While a handful describe themselves as moderate or pro-choice, most are unabashed pro-life conservatives with close ties to religious activists—47 had strong support from Christian conservatives. Not surprisingly, an overwhelming number favor abortion restrictions, prayer in schools, and taxpayer vouchers for religious academies.

Regionally, the 74 rookies shifted the GOP balance of power to the South and West from its traditional center in the Northeast and Midwest. Only 11 hail from the Northeast—the stronghold of moderate Republicanism—while 45 come from the Sun Belt. They picked Roger F. Wicker of Tupelo, Miss., as class president. This regional tilt explains their emphasis on states' rights, opposition to gun control, and support for private development of public lands.

The political profile of the freshman class should not be surprising, considering that most were recruited by Gingrich and his conservative associates at GOPAC, the political committee he ran from 1986 to 1995. After locating his new disciples, Gingrich gave them issue briefings, fund-raising help, and strategic advice, and lent a hand scripting their assaults on liberal Democrats and the "corrupt welfare state."

But the factor that made the freshmen a singular force was the Contract With America. The 10-point manifesto became a political bible for the new lawmakers. One, North Carolina's Myrick, pinned a laminated copy of it to her lapel when she arrived on the Hill. During the first hundred days of Republican rule, freshmen resisted attempts to water down the Contract and voted with the leader-

BUSINESS WEEK/HARRIS POLL

REFORMERS OR EXTREMISTS?

There's no doubt that the House freshmen have shaken up Washington. But Americans are divided over whether the newcomers are brave reformers seeking

fundamental change or inflexible extremists. A point of agreement: Americans are uniformly unimpressed with their take-no-prisoners tactics.

BESTED BY BILL

As you may know, a struggle between President Clinton and congressional Republicans over the federal budget has shut down the government twice. What is your opinion of the way in which each of the following has/have handled the budget negotiations and government shutdown. Do you approve strongly, approve somewhat, disapprove somewhat, or disapprove strongly?

	APPROVE STRONGLY	APPROVE SOMEWHAT	DISAPPROVE SOMEWHAT	DISAPPROVE STRONGLY	NOT SURE
President Clinton	16%	19%	26%	36%	3%
Senate Majority Leader Bob Dole	9%	21%	31%	30%	9%
House Republicans	12%	15%	28%	40%	5%
House Speaker Newt Gingrich	10%	14%	23%	45%	8%

A WAVE OF DISAPPROVAL

A group of 74 newly elected House Republicans is insisting that President Clinton agree to their version of a balanced budget, and has been willing to shut down the federal government to force an agreement. Do you approve or disapprove of what the House Republicans are doing?

Approve	26%
Disapprove	70%
Not sure	4%

DAMAGED IMAGES

Which of the following statements comes closest to expressing your opinion of the House Republicans and their role in the budget negotiations?

They are a new breed of politicians who are trying to keep the promises they made when they were elected instead of just wheeling and dealing and doing business as usual in Washington	49%
They are ideological extremists who are holding the federal government hostage because they are unwilling to compromise	45%
Not sure	6%

Survey of 755 adults conducted Jan. 5-8, 1996 for BUSINESS WEEK by Louis Harris & Associates. Results should be accurate to within 4 percentage points.

FEEDING FRENZY AT THE MONEY TROUGH

Las Vegas veterinarian John Ensign pulled off one of the big upsets of the 1994 congressional elections, toppling a four-term House Democrat in a Democratic district. Then, almost as soon as he arrived in Washington, Ensign turned his attention to 1996, mapping out a fund-raising strategy.

Using his powerful seat on the tax-writing House Ways & Means Committee as a lure, Ensign has held small dinners—at up to $500 a head—for health, energy, and banking lobbyists. He also has visited potential donors in Chicago and New York. Ensign's tenacity has paid off: During the first half of 1995, he raked in $195,854 from political action committees, tops among the GOP frosh. "We have one of the toughest races in the freshman class," he says. "We want to be able to respond to attack ads."

SCHMOOZING: *Riggs' war chest has discouraged a challenger*

Ensign isn't the only GOP first-termer with a golden touch. Although they stormed Capitol Hill promising to shake up the political Establishment, the Class of '94 has embraced one time-honored Washington tradition all too well: shaking the special-interest money tree. During the first half of 1995, the 74 GOP freshmen raised $4.8 million from PACs—49% of their total take, says Common Cause, a public-interest watchdog group. That's about $1.3 million more than the class of 1992 had raised during the same point in the election cycle and the most ever raised by a freshman class so early.

TROUBLESOME. Although lawmakers won't file Federal Election Commission reports for the second half of 1995 until Jan. 31, interviews with PAC managers and a spot check of recent PAC reports indicate that the giving only has accelerated. "The freshmen have raised 'working hard for the money' to a new level," says David Rehr, a lobbyist with the National Beer Wholesalers Assn.

What's behind their zeal? Fear. Freshmen are vulnerable when they seek reelection, and early money can scare off rivals. Take Representative Frank Riggs (R.-Calif.), whose $201,309 in PAC and individual donations has discouraged a '96 challenge by a popular state senator. Corporate interests yearning for a sympathetic ear on Capitol Hill, meanwhile, are happy to oblige. Among the top PAC givers: homebuilders and Realtors, who killed congressional attempts to force large mortgage players to shore up the weak thrift insurance fund; the beer wholesalers, who want to ensure that beer taxes do not rise; and cigarette companies opposed to anti-tobacco regulations (table).

Some first-termers are troubled by their colleagues' successful PAC fund-raising. "History will judge us on whether we clean up the mess or continue politics as usual," laments Representative Linda Smith (R-Wash.). Smith wants to outlaw PAC giving altogether—or at least to lower per-lawmaker contributions from the current $5,000. She and others grumble that GOP leaders have only given lip service to reform. Argues Ensign: "I can't dismantle unilaterally." Representative Sue Kelly (R-N. Y.) agrees. "I would be glad to get this monkey off our backs. But until finance reform happens, most of us will accept PAC funding. We have to run a race."

These freshmen, though, are far from passive recipients. Many court corporations with business before their committees. Take Representative Daniel Frisa (R-N. Y.), who sits on House Commerce. The committee is considering a telecommunications overhaul, but Frisa accepted more than $40,000 during 1995 from those with a stake in the outcome, such as AT&T, BellSouth, MCI Communications, and Nynex.

WHO'S ARGUING? Meanwhile, Representative Frank A. Cremeans (R-Ohio), whose Banking Committee is mulling a bill to make it tougher for banks to sell insurance, has received about $45,000 from bankers and insurers, including Banc One, NationsBank, and the National Association of Life Underwriters. "They've bought into the system, and the system has bought into them," says Joshua Goldstein of the Center for Responsive Politics, a campaign-finance research group.

With the '96 election looming, the money chase is sure to speed up. And no one has much interest in stopping it: neither the lawmakers who want to keep their jobs nor the companies that need a favor or two from them.

By Susan B. Garland, with Stephen H. Wildstrom and Amy Barrett, in Washington

BACKING THE FROSH

PAC	TOTAL AMOUNT GIVEN, FIRST HALF OF 1995
NATIONAL RIFLE ASSN.	$141,150
NATIONAL BEER WHOLESALERS' ASSN.	109,492
NATIONAL ASSOCIATION OF REALTORS	94,910
NATIONAL AUTOMOBILE DEALERS ASSN.	84,125
NATIONAL ASSOCIATION OF HOME BUILDERS	77,000
AMERICAN MEDICAL ASSN.	69,900
AMERICAN MARITIME OFFICERS	66,000
RJR NABISCO	65,500

DATA: CENTER FOR RESPONSIVE POLITICS

ship 99% of the time. "Maybe I'm crazy or maybe I'm dumb to say: When you make a promise to somebody, keep the promise," says Oklahoma's Watts.

While many of the freshmen owe their careers to Gingrich, the Speaker in many ways owes his iron gavel to his recruits. The former *enfant terrible* of the House GOP rewarded freshmen allies by placing them on powerful committees, and they responded by making sure the party's Old Bulls remained unwavering in their fealty to the Contract.

This symbiotic relationship with Gingrich gives first-termers unprecedented leverage over senior Republicans. When House Appropriations Committee Chairman Bob Livingston (R-La.) kicked freshman Mark W. Neumann (R-Wis.) off the defense subcommittee on Oct. 11 for the sin of refusing to back the panel's military-spending agreement, the rookies rebelled. At a meeting on Gingrich's balcony, freshmen noted that two senior Republicans, Larry Combest of Texas and Bill Emerson of Missouri, were not disciplined when they joined with Democrats to sink leadership-backed farm-spending cuts. Gingrich agreed to compromise; Neumann would leave Appropriations for another plum assignment, the Budget Committee.

How can a group of newcomers exert such sway over the most powerful figure on Capitol Hill? For one thing, their numbers. With a bloc of 74 votes—and 50 hard-core conservatives among them—the freshmen have enough nays to sink any proposals they oppose.

Just as important is their internal cohesiveness. The class meets every Tuesday afternoon, usually in a subterranean chamber under the west front of the Capitol. The agenda is a mixture of policy and politics, including floor strategy, issues briefings, exchanges of polling data, and discussions of reelection races. Their "federalist" bloc is drafting proposals to turn over more Washington programs to cities and states. And to counter Democratic charges that they are inflexible hotheads, they've created six "tiger teams" to peddle their message to the media. "We want to separate fact from fiction," says Oklahoma's Largent, a team captain.

"We're not waiting in line... Most of

NEWT'S SNUB. Freshmen also are part of the formal GOP leadership structure. Two are subcommittee chairs—a rare honor for newcomers—and Myrick and fellow frosh David M. McIntosh (R-Ind.) attend top-level strategy sessions as class reps. "Senior members are the last people to be conferred with now," crows Wamp. "We are the first."

That cocky attitude has helped the freshmen score some triumphs on the House floor. One was an effort by Rick White (R-Wash.) to broker a compromise to regulate smut on the Internet. White, whose district is home to Microsoft Corp., deftly bridged differences between family-values advocates concerned about cyberporn and businesses worried about potential criminal liability.

The freshmen also forced reluctant GOP leaders to tighten lobbying rules and limit lobbyists' gifts to lawmakers. At a November meeting in Gingrich's office, the newcomers rejected offers by Gingrich and Armey to schedule votes on reform proposals in early 1996. Led by Representatives Linda Smith (R-Wash.) and Sam Brownback (R-Kan.), they demanded immediate action. Privately, Gingrich considers the reforms marginal. But warned that his stance would alienate Perot independents, he heeded the freshmen. "We're not waiting in line for our turn to speak," says Smith. "Most of us aren't going to be [on the Hill] for very long."

Other freshmen projects have been more divisive. Among them: a proposal by McIntosh and three-termer Ernest J. Istook Jr. (R-Okla.) to limit lobbying by liberal groups receiving federal grants. GOP moderates buried the plan in the Senate. And the frosh irked party elders by pressing to kill off the Commerce Dept., new B-2 bombers, the National Endowment for the Humanities, and government subsidies to tobacco farmers.

"Senior [House GOP] members are the last peop

WAMP'S WORLD: *The Tennessean says hardball tactics will pay off in the long run*

Most of the time, Gingrich condones freshman freelancing. Representative Mark A. Foley (R-Fla.), who questioned Gingrich's controversial book deal with a publishing house owned by Rupert Murdoch, says Gingrich never retaliated. "He respects me for being open and honest," says Foley.

Personal jabs are one thing. But the Speaker is growing impatient with freshmen who desert him on crucial votes. On Jan. 9, he disciplined three of them for vot-

ng against his com-
promise plan to re-
pen the government.
The punishment: He
acked out of appear-
nces at mid-January
und-raisers.

Have the freshmen
earned a lesson? Not
et. McIntosh con-
demns Gingrich's
'outrageous" action.
'He has to stop this
rybaby attitude with
people who don't
gree with him," he
omplains. Democrats
re watching with
glee. Gingrich "creat-

n't going to be [on the Hill] for very long"

ed this monster," says
Representative Bruce
F. Vento (D-Minn.).
'Now he has to deal
with it."

IMPATIENT: *Washington's Smith demanded an immediate vote on lobbying reforms*

Given public oppo-
sition to their guer-
rilla tactics, many of the freshmen may not be back next year. Some 44 of the 74—largely those who won narrow victories on Democratic turf—face risky to almost impossible reelection races (map, page 27). Even during a Republican landslide, 43 of them took less than 55% of the vote. Clinton carried 33 of their districts in '92. And nine represent areas won by both Clinton and 1988 Democratic nominee Michael S. Dukakis. "These people are from districts that are not as conservative as they are," says Carleton College political scientist Steven E. Schier. "A lot of them are vulnerable."

What's more, about a dozen freshmen have been damaged by scandal or foot-in-mouth disease. The top dud: Enid G. Waldholtz of Utah, whose financial dealings and marital breakup are an ongoing political soap opera.

strategists concede that the party won't repeat its '94 record of zero incumbent defeats. But because of likely Democratic setbacks in the South, neutral observers say that 30 rookies must fall for the GOP to lose the House. Republican operatives insist that fewer than a dozen freshmen are in deep trouble. The big reason? Money (page 29).

MODERATION. Despite their promise to change business as usual in Washington, the freshmen have tapped the D. C. money machine for nearly $5 million during their first six months in office—the most cash ever raised by first-termers from political action committees. The bulging war chests have intimidated some would-be Democratic challengers.

The freshmen also are bolstered by continuing support from Perot's new Reform Party, which plans to endorse major-party congressional candidates in '96 while fielding its own White House hopeful. In 1994, Perot backers favored GOP House candidates by 2 to 1. And Perot sees no reason why that will change this year: "They certainly can expect a huge amount of support from independent voters," he says.

But even Perot's blessing won't rescue the rookies if they don't score some big policy victories, including a budget deal, welfare reform, and a campaign-finance overhaul. "The biggest risk is that the public perception of gridlock will hurt the Republicans in the fall," says Pitney.

Indeed, some endangered freshmen are starting to get the message. Flexibility that doesn't sacrifice bedrock principle is their new byword. They're trying to develop a bipartisan budget deal with moderate and conservative Democrats led by Gary A. Condit (D-Calif.).

While individual freshmen realize they must make some compromises, the class as a whole is not yet ready to yield on sticky issues such as welfare, Medicare restructuring, and tax cuts. "Some of them still operate on the assumption that only they have been to the top of the mountain and seen the promised land," jabs House moderate Sherwood L. Boehlert (R-N. Y.).

Moderates may well remain frustrated with the revolutionaries. Despite warnings from the center, many freshmen say they would rather try and fail than cut deal after deal with liberal Democrats. That could be a path to political self-destruction. After the Republicans' skillful '94 campaign, voters gave them a historic opportunity to change the direction of Washington. But unless these raw revolutionaries begin to develop a depth of political maturity soon, they risk becoming nothing more than a colorful but short-lived episode in American history.

By Richard S. Dunham, with Amy Barrett in Washington and bureau reports

be conferred with now. We are the first"

The tenuous grip of many freshmen has helped Democrats recruit top-flight challengers. Oklahoma House Speaker Glen Johnson is taking on freshman Tom A. Coburn. Debbie Stabenow, a former Michigan state senator, is going after freshman Dick Chrysler. And former Arizona Democratic Party Chairman Steve Owens has set his sights on J. D. Hayworth, an ex-TV sportscaster dubbed Rush Jr. because of his resemblance to the conservative talk show host.

Even the most optimistic Republican

DAN AMOUR MATRA

COMMENTARY

By Howard Gleckman

LESSONS FROM THE CLASS OF '74

Riding a wave of revulsion against politics as usual, a huge crop of newcomers sweeps into Congress. Promising to overthrow the old order, they demand broad changes to make Washington more accountable to ordinary citizens. The Republican freshmen Class of 1994? Nope, the Democratic Class of '74—better known as the Watergate Babies.

Despite their best intentions, the 75 House Democrats who rode the Nixon Administration scandals into office two decades ago failed to fundamentally change politics. Unable to work together as a unit and seduced by money and Washington perks, the Watergate Babies eventually were co-opted by the system. The current crop of freshmen risks failure as well. Their fatal flaws: hubris and an unwillingness to make the compromises governing requires.

While the two historic classes share huge size and reformist zeal, there are stark differences. The Class of '74 cut its political teeth as opponents of the Vietnam War, yet its members were pragmatists rather than ideologues. They largely rejected the sort of liberalism that resulted in their party's overwhelming defeat in the 1972 Presidential elections. They wanted to make government work better, not get bigger. And they tried to break the hold of unions and other special interests on the Democratic Party.

RESTORATION. By contrast, many of today's Republican freshmen want to defenestrate the federal government, not improve it. And rather than distancing themselves from special interests, such as the religious right, they have embraced them.

The biggest difference may be in the way each class tried to reform Congress. Both vowed to overthrow the cozy Capitol Hill power structure. But in the name of democratization, the Class of '74 created anarchy, while the Class of '94 has accepted the iron rule of House Speaker Newt Gingrich (R-Ga.). Although the Republican frosh occasionally buck the Speaker, they've voted with him a staggering 94%—and 99% of the time during the first 100 days.

ON NIXON'S HEELS: *The Watergate Babies tried to shake up Washington, too*

The Watergate Babies stripped power from the party kingpins. They dumped committee chairmen and changed rules so the party caucus, rather than the leadership, made committee assignments. Bucking the old bulls was easy because the Class of '74 owed little to the Democratic bosses. "We didn't expect a lot of the Watergate class to win," remembers Sam M. Gibbons (D-Fla.). "We just put them on the ballot to have a Democratic name there."

Gingrich, on the other hand, consciously went about constructing his majority by electing rookies, using the Contract With America and well-placed campaign funds as tools. While grateful GOP freshmen talk about a revolution, they actually have assented to a Restoration—a return to the days of all-powerful Speakers. Says University of Maryland government professor James Gimpel: "They've been willing to invest in Gingrich's moral authority to recentralize power in the House."

Today's freshmen have so far been happy to give the Speaker enormous power because they believe he can lead their push for radical change. That's far afield from the '74 reformers who hobbled their Speaker. As a result, they created a power vacuum that would be filled over the next decade by strong committee chairmen such as Ways & Means boss Dan Rostenkowski (D-Ill.).

CHECK BOUNCERS. Some of the Watergate Babies eventually gained powerful positions. Paul Tsongas (D-Mass.) and Paul Simon (D-Ill.), for instance, went to the Senate and eventually ran for President. Indeed, it was remarkable how easily much of this class adapted to Washington. They took generous campaign money. They bounced checks at the House bank. They became part of a system they had vowed to change when their hair was longer and their commitment deeper.

The Watergate Babies have left lessons for the GOP gang of Contract-quoting short hairs. The first: Beware of the seductive power of special-interest money. Already, new Republicans have collected more dough from special interests than any class in history. The second: Even the best intentions can backfire. The Class of '74's legacy was a campaign-finance reform law that created the very political action committees that many see as the root of today's ills. The Class of '94 is in danger of leaving a disappointing legacy of its own: It stood for principle but accomplished little.

Gleckman began covering Washington politics in 1977.

To launch Windows® 95, *they used* 4 networks, 85 magazines, 100 radio stations and, *ahem,* one server.

TO POWER THE ON-LINE LAUNCH OF WINDOWS® 95, MICROSOFT CHOSE THE DIGITAL PRIORIS™ HX 590DP SERVER.

Failure was not an option on August 24. Microsoft's official launch date for Windows® 95 marked the biggest new product introduction in industry history, not to mention one of the great all-out media blitzes. On this day, a minor glitch would have made headlines. So when all eyes turned to Microsoft—Microsoft turned to Digital.

For the on-line launch of Windows® 95, Microsoft plugged in the Digital Prioris Internet Server—ten of them, in fact. A decade of Microsoft/Digital teamwork was behind the decision. So was the simple realization that, for a job that meant handling almost two million hits the first day, the Prioris HX 590DP was simply the best server around. After all, its fault-tolerant features do include drive arrays, ECC memory, redundant cooling systems and power supplies. Put simply, Microsoft chose Digital for the same reasons you should. Reliability. Power. And no slip-ups.

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COMPUTERS

APPLE: TICK-TOCK, TICK-TOCK, TICK-TOCK...

Losses, shortages, stagnation–something's gotta give

There may still be a time bomb at Apple Computer Inc. The ugly news is out—a $69 million loss for the quarter ended on Dec. 29, some 1,300 layoffs, more wrenching reorganization. But critical questions still loom: Will Chief Executive Michael H. Spindler survive a Jan. 23 board meeting? And will Apple's nearly invisible board finally step forward and squelch lingering doubts about the company's future?

Apple directors aren't talking. But insiders say Spindler's job is in jeopardy. Current and former Apple executives also say the 53-year-old Spindler has been showing signs of strain. Insiders say he was wearing a heart monitor in the office the week of Jan. 8 and that, after a trip to the hospital, he worked from home for two days. A close friend says Spindler's chums have been urging him for months to slow down. Says the friend: "Michael is stressed. He's overweight. He doesn't eat right. He doesn't sleep right."

Such talk is triggering speculation that Spindler will leave the company for health reasons. Says one Apple executive who witnessed the heart monitor: "He is under incredible pressure." Spindler was unavailable for comment. An Apple spokeswoman says the company doesn't comment on employees' personal matters but adds: "Michael is here. He's fully engaged in the business. He was here all weekend [of Jan. 13]."

The question now is whether the reorganization Apple announced on Jan. 17 will fix what ails the company. The plan will pare the company's head count by 8% during the next year and may cause another net loss in the quarter that ends on Mar. 29. Apple also plans to more

SPINDLER: *Insiders say the CEO's job may go to a seasoned turnaround exec*

broadly license its Mac operating system and will consider selling some assets. But the plan falls way short of what analysts had hoped for. It "lacks decisiveness and thoroughness," says CS First Boston analyst C. William Gurley.

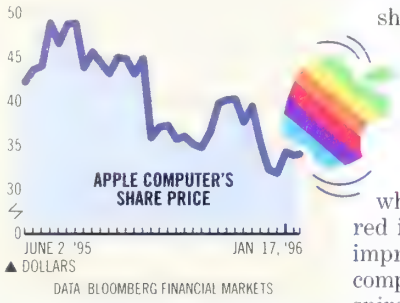
That keeps the pressure on Spindler. Apple has suffered three consecutive quarters of product shortages and then too much inventory—$80 million worth in the quarter ended on Dec. 29. It's locked in a bid for market share that has driven gross margins from 28.7% a year ago down to 15.1% today, below rivals Compaq Computer Corp. and Dell Computer Corp. What's worse, the effort isn't working: Apple lost market share in last year's final quarter, going from 8.2% to 7.1% of the world PC market, figures researcher International Data Corp.

FRONT-RUNNERS. Will Apple's board step in? Executives speculate that the directors may name their own CEO, most likely Apple director B. Jürgen Hintz, the 53-year-old former CEO of the $4.5 billion Anglo-French packaging company CarnaudMetalbox. He's credited with revitalizing Procter & Gamble Co.'s food business in the 1980s, when he worked there as executive vice-president, and then with boosting CarnaudMetalbox before it was taken over last fall. The thinking is that while Hintz lacks computer experience, he is a seasoned turnaround expert. Other Apple executives think board member Gilbert F. Amelio, CEO of National Semiconductor Corp., may be lured into the job.

How likely is either move? Outwardly, Apple's board gives few signs of taking drastic action. Says one director: "We're still supporting Michael. Apple has been through [tough times] on numerous occasions, and I basically believe it's a great company." But will the board let Apple lose more money in its market-share assault? "Not for too many quarters," says the board member. "You can gain market share all the way to the poorhouse."

The fact that the board would allow further losses at all troubles some analysts, who argue that more red ink would give the impression that the company is in a death spiral. That could

SOUR PERFORMANCE



DATA BLOOMBERG FINANCIAL MARKETS

prompt software companies to abandon Mac software development and shake he faith of Mac's loyal customers. Says ne insider: "You've got to blame this oard for not taking decisive action."

One problem, critics say, is that too nany board members are newcomers o Apple and the computer industry, in-luding Hintz, Katherine M. Hudson, EO of W. H. Brady Co., and Delano E. ewis, CEO of National Public Radio. ays one former Apple executive: "The oard is pretty weak. They've let this hing go way too long. They had plenty f warning signs.... They didn't do their lue diligence."

STRONG SHADOW. The board's king-naker is Chairman A. C. "Mike" Mark-ula Jr., who has been a staunch Spin-ller supporter. Markkula, who ran the ompany when it hit hard times in 981, is not as active in managing Ap-le today as he has been in past crises, ources say. He lunches with Spindler nd talks to him regularly, but he has et to meddle much. But his opinion ounts big-time: He made the calls to lump previous CEOs Steve Jobs and ohn Sculley.

Some investors are nervous about the oard because key members are selling pple stock. Markkula dumped 58,000 shares this summer ust after a 10% dip in price. He still owns 2.9% of Apple's hares, but that was his iggest sale ever. Longtime oard member Peter O. Crisp ollowed suit, selling 50,000 shares t around $40.

The latest restructuring may not elp soon. Analysts say that by lashing operations outside its seven op-selling countries, trimming ad-ministrative costs, and simplifying its roduct line, Apple could save about 120 million this year. That, combined ith a plan to ease out of the low end of he market, could keep the Mac busi-ess healthy without fouling Apple's bot-om line. Says Tim Bajarin, president of reative Strategies Inc.: "I believe they inally have the right business model."

Win or lose, it won't be a pretty tran-ition. But Apple still has a lot going or it—including fiercely loyal custom-rs, dominance in the education market, nd a strong brand name. "Apple has ssets other businesses would kill for," says Compaq Chairman Benjamin M. Rosen, who engineered an epic turn-round when his company faced similar roblems in 1991. A friend of Markkula's, he thinks Apple's problems can be over-ome. But not without bolder moves—either by Spindler or his board.

By Peter Burrows, with Kathy Rebello, in San Francisco, with bureau reports

FOOTBALL

READY, SET, TACKLE THAT CEO

Arizona's elaborate plan to woo companies at the Super Bowl

Sometimes the Big Game doesn't happen on the field. So it is with Super Bowl XXX, the annual gridiron classic that will pit the Dallas Cowboys against the Pittsburgh Steelers on Jan. 28. For Arizona officials who will host the game on the Arizona State University campus in Tempe, the real blitz won't be from linebackers but from high-profile recruiters charging the nation's top chief executives.

Most cities that host pro football's extravaganza are content to welcome tourists and their money. Arizona's game plan: to entice CEOs into relocating their companies after the final whistle blows. Officials already have identified more than 500 chief executives or other business leaders—"decision-makers" in Arizona booster-speak—who will attend the game and have been targeted to receive special treatment. "The idea is to show that we're more than just a place with nice weather and clean air," says Arizona Governor Fife Symington.

It's the most extensive business recruiting effort ever attached to the Super Bowl, say National Football League officials, outdoing even the splashy economic-development-minded welcome mounted for last year's championship in Miami. The Arizona host committee has focused on the 60 most likely prospects and is linking each of them to Arizona CEOs (known as "mentors"). The host committee has booked reservations for them at hard-to-get-into restaurants, golf courses, and hotels. And on Super Bowl Sunday, a fleet of helicopters will whisk them from a private golf event to the stadium.

The effort comes after Arizona got the game in the equivalent of a civic Hail-Mary pass. In 1991, the state was bounced as the site for the 1993 Super Bowl after voters rejected a referendum on a state-paid Martin Luther King Jr. holiday. That cost Arizona an estimated $200 million in convention revenue as well. Officials won the game back in 1993 with a vow that a King holiday would be forthcoming. Little wonder: Super Bowl XXX is estimated to bring in some $187 million in tourist revenue.

Give Arizona credit for knowing how to sell itself. Last year, it lured 80 companies, including an animation studio for Twentieth Century-Fox Film Corp. and a BankAmerica Corp. credit-card unit. In all, Arizona imported 16,000 new jobs last year, says its Dept. of Commerce.

What effect will the Super Bowl have? The Broward (Fla.) Economic Development Council doesn't know of any corporate relocations to South Florida resulting from the 1995 Super Bowl. And "you have to wonder if someone coming to the Super Bowl for a fun time is going to want a sales pitch," says Jack Kyser, chief economist for the Los Angeles Economic Development Corp. Side bet: How many CEOs will move their digs to Arizona once the game has ended? The early line is not in Arizona's favor.

Ronald Grover in Phoenix, with Gail DeGeorge in Miami

GAME TIME Some 500 CEOs will watch Kevin Greene and his Pittsburgh Steelers in Tempe on Super Sunday

DOUG HOS NUTRAL SPORT

EXECUTIVE SUITE

THE CEO WHO NEVER SLEEPS

Succession questions at Reed's restless Citi

REED: *More changes are afoot in consumer banking*

The early 1990s were dark indeed for Citicorp. Low on capital and contending with mounting loan losses, Citi faced almost daily rumors that Chairman and Chief Executive Officer John S. Reed was about to step down, either at the behest of Citi's board or of regulators. As part of the struggle to get the bank back on track, Reed abandoned Citi's traditional hierarchical structure. He made 15 business heads around the world report directly to him, flying into New York for monthly reviews of their progress toward tough performance goals.

Slowly, and with major assistance from low interest rates, Reed and his team have righted Citicorp. On Jan. 16, it reported record earnings of $3.46 billion for 1995. Citi has amassed some $18.9 billion in equity capital, up from $8.5 billion, using the same standards, in 1991.

HOUSECLEANING? Now, Reed's management structure is being dismantled. On Jan. 12, Vice-Chairman Pei-yuan Chia, 56, head of global consumer banking, announced his impending retirement, just a month after Vice-Chairman and turnaround expert Christopher J. Steffen, 53, head of finance and administration, abruptly resigned amid differences with Reed. Meanwhile, Reed has promoted a crop of business chiefs and hired William Campbell, former head of Philip Morris USA, to run branch banking.

Was it a housecleaning by Reed, or a flight of top-notch hands? A Citi spokesman says Chia is "retiring on his own terms." Reed, who told analysts on Jan. 16 that Chia will stand for board reelection this spring, also said that he and Chia had discussed the vice-chairman's retirement for several years. One source close to Citi, though, says Chia told him he was urged to resign. And a Citi insider says that the departure of Steffen was unexpected.

The suddenness of the announced changes surprised and disconcerted many Citi-watchers. Some wonder whether Reed, 56, is pushing some of his best executives out to ensure that no strong second-in-command emerges. "Whenever [Reed] gets someone with the potential to be a voice from below, those people have not lasted that long," says an analyst who was unwilling to be named. For example, in 1992, President Richard S. Braddock abruptly left the bank, and many believe Reed was defensively ousting his only credible potential successor as CEO. Reed refused interview requests, and a spokesman declined to comment.

The question now: Are any of the newly promoted executives capable of running Citi? Reed professes confidence. He told analysts on Jan. 16 that "very consciously, we are continuing to put emphasis on building the next generation of management." Accordingly, Rana Talwar, 47, formerly head of Asia/Pacific consumer banking, will run retail banking in Europe and North America. Victor J. Menezes, 46, former head of European and North American consumer banking, became chief financial officer when Steffen left. And Roberta J. Arena, 48, head of credit cards in North America and Europe, now reports directly to Reed. These executives are very well regarded—but it will take time for them to develop the broad managerial experience Reed seeks.

"LEADERSHIP VOID." Meanwhile, the departure of Chia will leave a gap. Along with Reed, he made Citi the preeminent global consumer bank. Says Merrill Lynch & Co. analyst Judah Kraushaar: "To lose somebody [at that level] potentially creates a leadership void." In addition to Chia, David E. Gibson, 55, head of emerging-markets global finance, will retire in March.

Reed told analysts that more changes are in the offing, particularly in consumer banking. And the shifts, which seem to be endemic to Reed's restless management style, may continue for some time. Reed is unlikely to step down any time soon, says David S. Berry, director of research at bank specialists Keefe, Bruyette & Woods Inc. "Why would he leave? It's got to be more fun than it was four years ago." Particularly when, instead of listening to rumors about his own departure, he can shuffle other executives around.

By Kelley Holland in New York

SHUFFLING FROM THE TOP OF THE DECK

Some recent management changes at Citicorp

WHO'S OUT

PEI-YUAN CHIA, 56, vice-chairman in charge of global consumer banking, retiring by the end of 1996

CHRISTOPHER STEFFEN, 53, vice-chairman in charge of finance and administration, resigned abruptly in December

DAVID GIBSON, 55, chief of corporate banking for emerging markets, retiring at the end of March

WHO'S IN

ROBERTA ARENA, 48, head of the credit card business in Europe and North America

WILLIAM CAMPBELL, 51, formerly head of Philip Morris USA, hired to run branch banking worldwide

VICTOR MENEZES, 46, promoted to chief financial officer in December; was head of European and North American consumer banking

DATA: BUSINESS WEEK, COMPANY REPORTS

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COMMENTARY

By Richard A. Melcher and Greg Burns

ARCHER DANIELS' CLEANUP: DON'T STOP NOW

Only at Archer Daniels Midland Co. could a corporate-governance revolution occur in the chairman's basement. On Jan. 14, ADM directors filed down the steps at Dwayne O. Andreas' Decatur (Ill.) home to discuss Agenda Item No. 1: whether to enact sweeping changes that could turn the insider-dominated group into a model of independent oversight. At the next day's regularly scheduled board meeting, the group O. K.'d the plan without dissent.

If the board actually puts into practice what it has approved on paper, ADM could catapult from a company regularly shellacked by investor activists to one of exemplary corporate openness. At the very least, a half-dozen of ADM's 17 directors will likely step down by October's annual meeting, paving the way for more outsiders.

FBI MOLE. ADM's board upheaval stems from investor concern that its cloistered leaders fostered a culture of hubris that may have encouraged executives to stray into illegal activities. Until last summer's news of a federal investigation into alleged price-fixing of three important ADM products, corporate-governance issues were as unwelcome at the agribusiness giant as corn blight. After a former executive admitted to being an FBI mole, restless shareholders loudly proclaimed their dissatisfaction with a board controlled by Andreas family members, former executives, and relatives of senior management. Often, misguided strategies prompt shareholder revolts. "Something usually triggers it," says Ray A. Goldberg, a Harvard business school professor and ADM director who co-chaired the board committee that wrote the company's governance report. "Unfortunately, for this company, it was an antitrust investigation."

The document, produced after three months of study, addresses most key shareholder concerns. During the process, the committee held discussions with such influential activists as Sarah Teslik, executive director of the Council of Institutional Investors, a body representing big pension funds.

Among the main recommendations in the report:

- The board should be cut to as few as nine members, the majority being outsiders.
- Management should be limited to three seats, down from five.
- Committees should be entirely composed of outsiders, except for the executive committee.
- Outside directors should step down at age 70.

A new nominating committee headed by an outsider—for now, Democratic Party heavyweight Robert S. Strauss—could break the Andreas family's lock on many key executive positions. Since Andreas is turning 78, the board needs to establish a succession plan—and they might logically extend their search beyond the present heir apparent, Dwayne's son, Vice-Chairman Michael D. Andreas.

For true reform to take place, Archer Daniels must really dig in and clear out. Even former Chairman John H. Daniels, 74, favors paring the board by the maximum recommended. Daniels plans to step down, as do Goldberg and Happy Rockefeller. Other directors who may be heading for the boardroom exits: former ADM executives Lowell W. Andreas (Dwayne's brother) and Ralph Bruce, and investor Shreve M. Archer Jr. (father of ADM treasurer Charles P. Archer).

Once the board has been revamped, it should reward long-suffering shareholders. The company should boost its dividend from the present measly 1.1% and extend its recent share-buyback initiative. With nearly $1 billion of free cash, ADM can well afford to spread the wealth among its investors without limiting the company's financial flexibility.

The company should also resolve several open-ended issues. It needs to adopt a rigid definition of outside directors, taking a hard line on any personal or business connections that could even give the appearance of conflicts. Strauss, for instance, whose Washington law firm does business with Archer Daniels, should not be allowed to pass himself off as an "independent" director.

INGRAINED

If the board follows through, shareholders will reclaim a public company that has been run as a family fiefdom

ENDLESS REIGN. Plus, ADM needs to establish a strong "lead" director as a counterweight to Andreas and to help attract a diverse new set of directors to face stepped-up global competition. Says ex-Chairman Daniels: "We're no longer just a little flour-milling company." For now, forget about splitting the CEO and chairman posts, another suggestion the directors include in the report. The company could never attract a strong chief executive to serve under the strong-willed Andreas—who shows no sign of retiring as chairman.

Archer Daniels Midland should be commended for its latest move. But it still has to convince investors that it is finally playing by the rules that govern most of Corporate America rather than the Andreas rules that have prevailed for years.

Melcher and Burns follow Archer Daniels Midland from Chicago.

RESEARCH

A RACE TO SQUASH THE SUPERBUGS

Drugmakers finally go after the lethal new microbes

It's a chilling notion: deadly bacteria that drugs can't kill. These "superbugs" almost claimed the life of a 55-year-old diabetic being treated for a blood infection last winter at New Jersey's East Orange V. A. Medical Center. Doctors tried their most powerful antibiotics, yet nothing would defeat the relentless microbe.

Fortunately, Lisa Dever, chief of the hospital's infectious diseases clinic, was testing an experimental agent from Rhône-Poulenc Rorer called Synercid. She used it on the fading patient, who after two weeks of injections emerged cured. Dever says the compound can zap other seemingly invulnerable killers that cause, among other things, pneumonia and meningitis.

After years of doing little to combat superbugs, giant pharmaceutical companies once again are putting their muscle into multimillion-dollar counterattacks. Rhône and other drugmakers, including Upjohn, Pfizer, Schering-Plough, and Eli Lilly, are improving older antibiotics, racing new ones through clinical tests, and fine-tuning methods to identify and screen new drugs faster. To bolster their efforts, they're forging partnerships with science labs and biotech startups that are expert in drug-resistant microbes. In December, for instance, Schering-Plough Corp. said it would sink $44 million into Genome Therapeutics of Waltham, Mass., which is

TOMASZ: *The microbiologist was one of the first to sound the alarm about drug-resistant bugs*

searching for genes that coul chinks in the bacteria's armo

The need for new drugs c not be more urgent. In 1985, 0.02% of infections around U. S. showed resistance to cillin, says Rockefeller Unive microbiologist Alexander Tom who was one of the first to s alarms. By 1993, drug-resis infections were killing 1(Americans a year.

What has rendered peni and other time-honored bl busters impotent? Scien blame the explosion of dru sistant microbes on everyt from overuse of antibiotic medicine and agriculture to spread of invasive surgical cedures to urban crowding.

Drugmakers themselves deserve censure. According to industry mag *Scrip*, 50% of antibiotics manufactu in the U. S. and Japan curtailed dev ment in the mid-1980s, assuming vi in the battle against microbes.

In the race to recoup lost ground first important new drug on the shelf be Rhône's Synercid. It could win Fo Drug Administration approval for uses as early as 1997, if the agency ag to fast-track clearance. Close behi

HEALTH CARE

AN HMO GAMBLE FOR COLUMBIA?

It's eyeing Ohio Blue Cross' managed-care operation

For years, hospital monolith Columbia/HCA Healthcare Corp. has vowed it would stay out of the insurance business, spooked by the debacle that attended Humana Inc.'s attempt in the late 1980s to consolidate acute medical-care and health-maintenance organizations. That effort crashed, forcing Humana to spin off its hospitals into a company later devoured by the acquiring Columbia dervish.

The health-care landscape, though, has shifted dramatically—and Columbia has become a $17 billion behemoth with the sort of clout that allows it to change its mind. In Cleveland, where it has a half-share in two hospitals, the company is in advanced negotiations to take over a joint venture controlling the managed-care operation of Blue Cross & Blue Shield of Ohio, according to a source close to the talks.

The deal could create an integrated system funneling more than 400,000 plan members into seven Ohio hospitals controlled by or linked to Columbia. More significant, the move into insurance would signal a turning point for the $700 billion health-care industry, likely transforming the ongoing pursuit of bulk through acquisition into a race as well for soup-to-nuts vertical reach. "We'll see hospitals going to bed with two or three other hospitals and then buying their own managed care," says Princeton University Professor Uwe Reinhardt.

LUDICROUS. Both Columbia and Blue Cross & Blue Shield of Ohio refuse to confirm their talks. While admitting that Blue Cross & Blue Shield is discussing some sort of deal with two companies, a spokesman says the idea of abandoning its managed care joint-venture is ludicrous: "The dumbest thing in the world would be to sell off your biggest marketplace." Peter Reibold, president of Columbia's Ohio division, only points out that "the company is open to discussions with a variety of organizations."

In fact, Columbia says it is eyeing 150 hospital acquisitions worldwide. Entering the HMO busi though, would be another matter– filling a fantasy hospital executives enjoyed for as long as managed care drained their revenues. Theoreti hospitals with captive HMOs could by insurers, selling medical care direct employers. A few have pulled off ventures, but it has proven difficul Humana's case, rival insurers sent patients to other hospitals, and do resisted HMO cost-cutting efforts.

Today, though, "there's a greater of acceptance of managed care from tors, and it may be worth the ris

of compounds called oxazolidinones, Upjohn has developed to jam the bugs' ability to multiply. And Lilly is ving vancomycin, one of the few ef- e superbug-busters. It seeks expe- FDA approval for a new version that ɔe 100 times more potent.

T PICTURE? As strong as the need is ıe new drugs, however, their profit tial is unclear. A drug typically costs . $200 million to develop. Merrill ı & Co. senior analyst Richard : says patients may not take enough : superbug fighters to bring a com- financial reward—only up to 15 days' ı to defeat drug-resistant bacteria, ars for the drugs that fight chronic lies, such as hypertension.

ysician Dever argues that a single -spectrum antibiotic from Merck & alled Primaxin, can account for as as 10% to 20% of a hospital's phar- budget—and isn't even effective st many resistant strains. And man- ırers can charge a premium for new- ore powerful compounds. Better ology also should bring down costs. the battle of drug companies vs. ıicrobial kingdom, the good guys gained some ground. But the war is y won.

Neil Gross in New York, with John ı in Washington

ıvating your competitors," says ı-care consultant William F. Nors- ıy. Moreover, Columbia, with 340 tals, has leverage with insurance anies that no company could claim a e ago. In Florida, for example, it ontracted directly with Wal-Mart s to provide employees hospital

leed, competing managed-care com- s haven't been pleased by rumors of nbia's impending deal. "There will nger be a level playing field," says ıel Eleff, chief medical officer of Aet- ealth Plans of Ohio, which covers 350,000 people in the area. Yet Aetna is angling to create its own integrated systems by buying up doctors' groups; other insurers are adding hospitals. The health-care business, already in the throes of a monumental consolidation, is about to see some real action.

By Nicole Harris in Atlanta and Zachary Schiller in Cleveland

ENT PLAN

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AUTOS

THE LITTLE CAR THAT COULD CARRY CHRYSLER OVERSEAS

A secret plan marks a strategic shift toward emerging markets

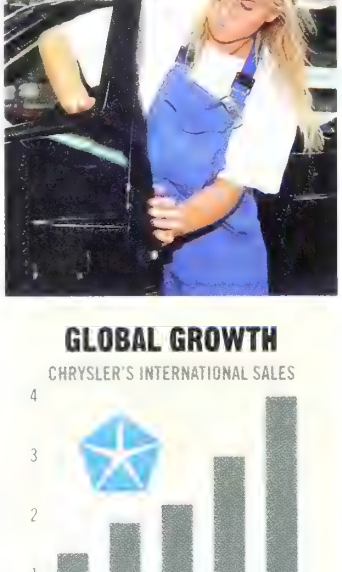
It's a project Chrysler Corp. executives talk about discreetly, if at all. They call it the BTV—a "basic transportation vehicle" aimed at developing nations in Asia and South America. It's under wraps for now, but the tiny car eventually could be Chrysler's secret weapon in the global car wars.

The hush-hush BTV is an important symbol of Chrysler's plans for a bigger push into overseas markets. The No. 3 U. S. car company is talking with India's Bajaj Auto Ltd. and Germany's Daimler Benz about forming overseas joint ventures, perhaps to build the BTV and perhaps for other projects. "We've looked at joint ventures in China and India," says Jürgen Hubbert, a member of the management board at Daimler's Mercedes-Benz unit.

BIG SHIFT. The talks come on top of a recent expansion effort overseas. This spring Chrysler is opening a European headquarters in Brussels that will have a staff of 200 by next year. It also is quietly putting up small assembly plants in Argentina and Thailand, reentering the Vietnamese and South African markets, and planning what Chairman Robert J. Eaton calls a "very sizable operation" in Brazil. Chrysler already has a five-year-old joint venture in Austria with an Austrian engineering firm that builds minivans and Jeep Grand Cherokees for sale in Europe. And it is developing a distribution network that will be selling right-hand-drive Grand Cherokees, Neons, Jeep Wranglers, and minivans in Japan by yearend.

The global moves mark a major shift in Chrysler's strategy. The company's foreign sales dropped to about zero after it sold off its European operation when it was struggling for survival during the late 1970s. Since surviving another brush with bankruptcy in 1991, the company has nearly tripled international sales over four years, to $4 billion (chart). But that's still just 9% of sales, and Eaton wants to raise the figure to 15% by 2000.

The moves abroad could address one of dissident shareholder Kirk Kerkorian's main criticisms of the company. Kerkorian has attacked Chrysler for its weakness in overseas markets and likely will approve of the expansion as long as it can be carried out relatively cheaply. But Chrysler insiders are bracing for criticism from Kerkorian if they go ahead with a major BTV plant, which could cost $1 billion or more and would cut into profit margins. "This is not the sort of thing an impatient shareholder wants," admits a top Chrysler insider.



ON THE LINE IN AUSTRIA: *Building Cherokees and minivans for Europe*

The BTV is important because it would allow Chrysler to home in on some of the world's fastest-growing markets. The idea is to appeal to buyers in developing nations in Asia, Africa, and Latin America with a car that is smaller and cheaper than models currently available. Chrysler already has crafted crude mock-ups of the four-seat BTV, which would sell for a minuscule $4,000 to $6,000 and would be even tinier than the urban commuter cars Ford and other rivals are developing for Europe. Insiders say the company hasn't decided for sure whether to build the BTV, but they acknowledge that coming out with such a vehicle is one of the company's strategic goals.

Outsiders don't think that Chrysler can afford to dally. "To be a real volume player [internationally], Chrysler needs to have a true, entry-level vehicle," says DRI/McGraw-Hill analyst Lincoln C. Merrihew. The BTV might be just the product to put a little gas into Chrysler's overseas comeback.

By Bill Vlasic in Detroit

EDITED BY THANE PETERSON

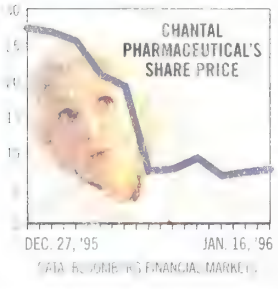
WAL-MART: A STRING SNAPS

OUCH. AFTER EARNINGS GAINS for 99 straight quarters, Wal-Mart said on Jan. 17 that weak holiday sales and intense competition will cause its fourth-quarter profits to drop as much as 11% from the same period a year ago. Analysts expect the retailer to earn $97 million on sales of $27 billion for the quarter. More bad news for Wal-Mart comes from China. Joe Hatfield, Wal-Mart's chief operating officer for China/Hong Kong, confirms that Wal-Mart's once-promising joint venture with Thai conglomerate Charoen Pokphand Group to operate discount stores in China has fallen apart. Industry sources say the partners couldn't decide who would be boss. Wal-Mart now plans to open stores in China on its own.

CLOSING BELL

BAD WRINKLES

Lately, Chantal Pharmaceutical can't get a break. Its shares rose twelvefold in 1995, to 27¼, making it one of the hottest stocks around. Now, it has tanked to about 8. First, Johnson & Johnson got a federal O. K. on an anti-wrinkle drug that competes with Chantal's main product. Then, *Barron's* printed a critical story about Chantal's finances. Now, short sellers are piling on. Founder Chantal Burnison has asked the SEC to probe what she calls "vicious rumors" and "outright lies" about her and the company.



BIONDI GETS THE BOOT

VIACOM CEO FRANK BIONDI was ousted unexpectedly on Jan. 17 from the company he had helped build into an entertainment giant. Biondi and Chairman Sumner Redstone had clashed over Biondi's laid-back management style for some time, says a source close to the situation, and Viacom's disappointing summer films and lagging share price didn't help. The board, advised of a special meeting to decide the issue only the night before, voted unanimously to boot Biondi. Redstone will take on the company's CEO duties. "Frank's great. But with the challenges we have, we need a more entrepreneurial, hands-on" style, Redstone says.

DUELING TITLES AT AT&T

IS ALEX MANDL AT&T'S NEXT chairman? Or John Zeglis? Mandl, 52, became the favorite on Jan. 17 when 60-year-old Robert Allen named him president and chief operating officer, effective after AT&T splits into three parts sometime before the end of 1997. Mandl was also named to a new "chairman's office" and chairman of a new Global Operations Council. But chief counsel Zeglis picked up titles, too: He becomes a senior executive vice-president, chairman's office member, and head of a new Executive Policy Council.

A FED INFLATION DOVE FLIES AWAY

THE CLINTON WHITE HOUSE IS losing a friend at the Fed. Vice-Chairman Alan Blinder has told the President he won't seek renomination when his term ends on Jan. 31 but will return to teaching at Princeton. A self-described "inflation dove" who believed the central bank should be mindful of keeping unemployment low, Blinder privately argued against the last of the Fed's seven rate hikes in late 1994 and early 1995. Fed watchers say his public warnings about the softening economy helped spur Chairman Alan Greenspan to cut rates last June and December. Rumored replacements include Comptroller of the Currency Eugene Ludwig, Harvard's Benjamin Friedman, and Princeton's Peter Kenen.

LABOR RINGS A BELL

CHALK UP A RARE VICTORY for labor. The Communications Workers of America has mainly bested Bell Atlantic in a new contract carved out in mid-January. The company had resisted terms agreed to by other Baby Bells last August. The union spent some $7 million on TV and radio ads to pressure Bell Atlantic. The deal, which the two expect to announce by late January, limits Bell Atlantic's right to subcontract work and set up lower pay scales for cable-laying jobs. Pay increases are similar to those at rival Bells, including wage hikes of more than 10.5% over three years.

HEADLINER: STEPHEN WOLF

BACK IN THE COCKPIT

If airline exec Stephen Wolf ever pens a management book, it'll have three chapters: 1) Extract worker concessions by threatening to dismantle the company. 2) Sell the company. 3) Cash out royally. That's what experts figure he'll do at USAir, where he was named chief executive on Jan. 16.

Wolf employed such a strategy at Republic Airlines and at Flying Tiger; he sold United Airlines to employees in 1994 before departing with $10 million in cash and stock options. Former colleagues were surprised that the turnaround ace, 54, would jump back into the cockpit so soon. After leaving United, Wolf seemed eager to spend time restoring vintage Jaguars, running his foundation for poor youths, and touring Paris cafés.

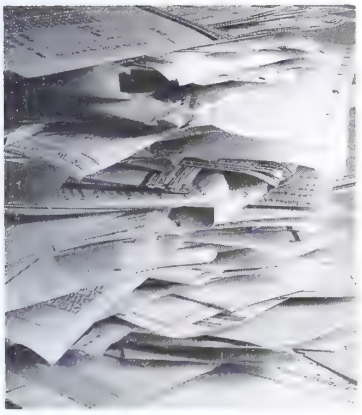
Why go back to work so soon? One ex-colleague thinks Wolf wants to dispel his image as a bad guy. But Wolf may face his toughest foe yet in USAir's unions. "Obviously Wolf is going to beat up on employees, and it's our job to stop him," warns Ken Thiede, chief of the airline's machinists' union.

By Dean Foust in Washington

ET CETERA . . .

- Air-kisses dept.: Helen Gurley Brown will step down as *Cosmopolitan* editor.
- Reebok plans to sell its Avia athletic shoe unit; it says markdowns hit '95 profits.
- McDonald's plans to buy back up to $2 billion worth of its shares over three years.
- Boeing and McDonnell Douglas have called off their merger negotiations.

Just because your portfolio is diversified doesn't mean it has to be all over the place.



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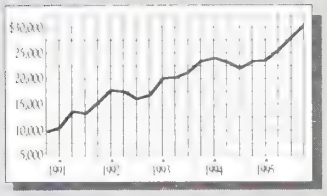

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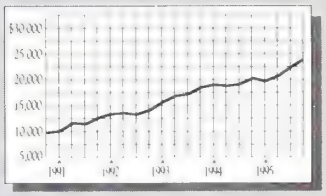

Value of investment: $24,180
Average annual returns (as of 9/30/95):
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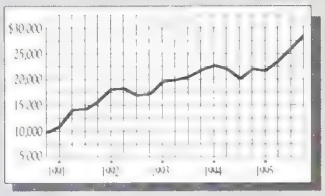

Value of investment: $28,702
Average annual returns (as of 9/30/95):
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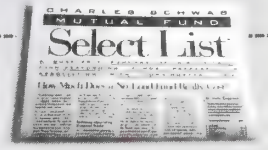
10 year +17.45%

MORNINGSTAR *Data provided by Morningstar, Inc. as of 9/30/95. These and over 350 funds are available through Schwab's Mutual Fund OneSource.*



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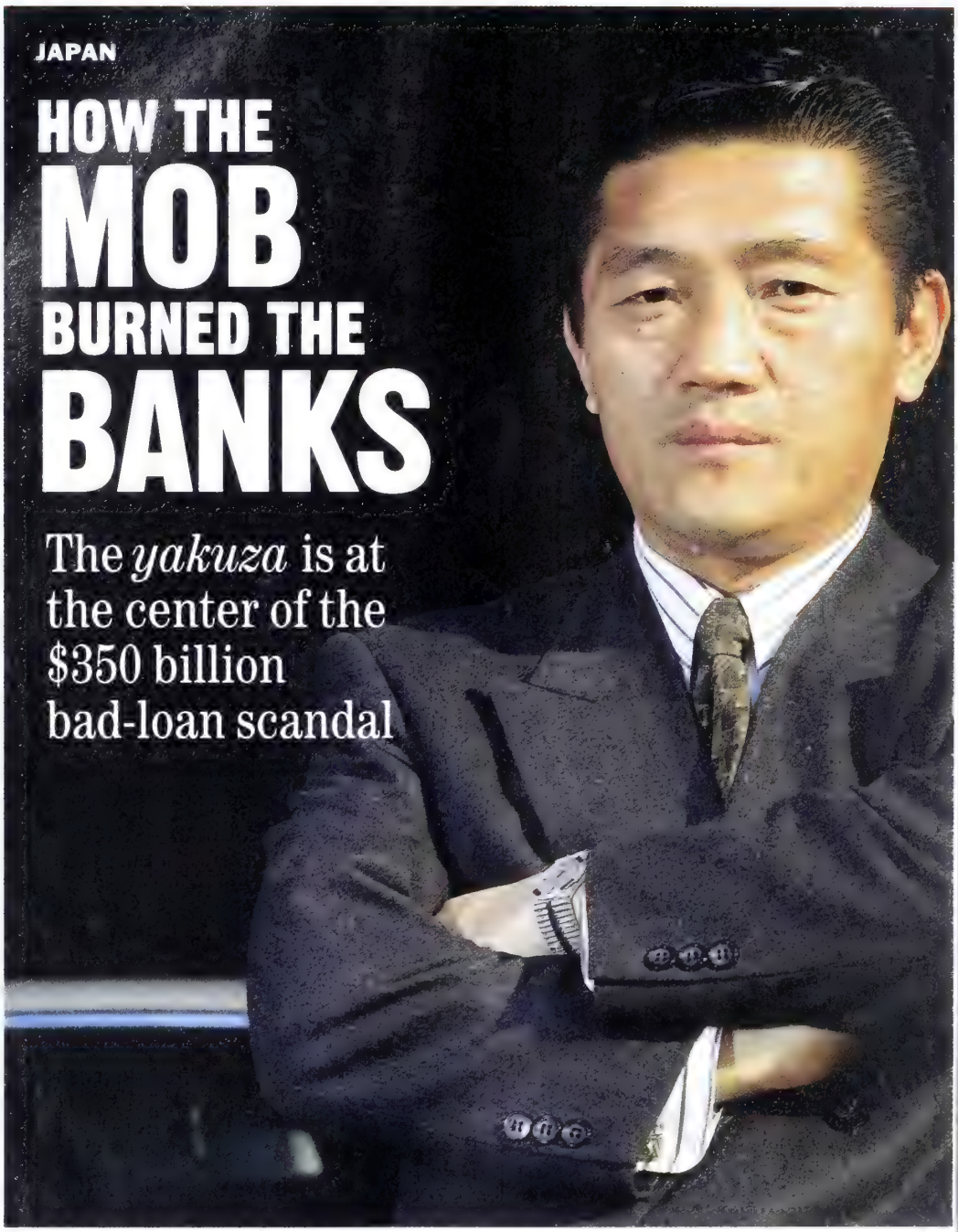
JAPAN

HOW THE MOB BURNED THE BANKS

The *yakuza* is at the center of the $350 billion bad-loan scandal



FORMER STRONG-ARM MAN HIROSHI ASAJI: *"I haven't done anything illegal—recently"*

With his chiseled facial features and cinder-block build, Hiroshi Asaji looks menacing without much effort. As a self-proclaimed "land turner," he was hired by property speculators in Osaka to force reluctant owners into selling lucrative sites during Japan's 1980s real estate boom. His tactics? Everything from placing blaring stereo speakers next to the house of a stubborn resident to hiring a gang to crush six ribs of another owner. Asaji makes no secret of the fact that he sometimes committed crimes and worked closely with the *yakuza*, Japan's criminal gangs, an account confirmed by the Osaka police.

Since those days, Asaji, now 47, has diversified his business network, the Koyo Group, into finance lending, real estate speculation, and love hotels, where couples can quietly take rooms. Some of Asaji's business activities are legitimate, others borderline. And although Asaji had to sell off seven real estate holdings in Osaka and Tokyo to pay down $300 million in debts when property prices started to collapse in 1991, he isn't exactly hurting.

On a blustery winter evening, an engaging Asaji escorted a visitor in his Mercedes-Benz 600 (he has a Rolls-Royce, too) to an opening bash at his new *nabemono*, or pot-bowl restaurant in central Osaka. Staff who had already gathered there hastily dropped their chopsticks, clicked off their cellular phones, and greeted him with a flurry of deep bows. Why is Asaji so forthcoming about his underworld connections? "This isn't a secret in Japan, and besides, I haven't done anything illegal—recently," he laughs.

Asaji isn't the only shady operator lurking in Japan's financial system. As the nation attempts to come to grips with its $350 billion bad-loan mess, it suddenly is becoming clear that the *yakuza* played a major role in creating the "bubble economy" of the late 1980s, when land and stock prices doubled and trebled. Taking advantage of the speculative fever of the era, gangs migrated from the shadowy periphery of the economy, where they concentrate on prostitution and drug-running, right into the heart of its financial system. As much as 10% of the bad loans officially recognized by the Ministry of Finance—or $35 billion worth—are now believed to have gone to the *yakuza*, figures Raisuke Miyawaki, a former investigator and corporate adviser on the gangs. Some estimates put the total amount of bad loans much higher, at $800 billion.

All this helps explain why the banking mess has proved so intractable—and why the government's new moves to bail out some failed financial institutions with an initial $6.8 billion public contribution are so controversial. Taxpayer dollars are going to be used to re-

build a banking system that can't recover on bad loans because the *yakuza* refuse to repay. In effect, Japan is embarking on perhaps the first-ever taxpayer-financed debt forgiveness of a nation's criminal underworld.

The all-powerful Ministry of Finance, which lords over every aspect of the nation's financial life, is attempting to portray the *yakuza* as key culprits in the post-bubble debt overhang. It's true the *yakuza* won't repay many loans they received from credit unions, housing-loan corporations, and real estate companies—and terrified lenders are afraid to press the issue too far. There have been 20 attacks reported against Japanese financial and corporate executives since 1994, including gangland-style executions of Sumitomo and Hanwa bankers who were trying to collect.

HOT POTATO. But one reason someone such as Asaji is willing to come forward is that the *yakuza* didn't create the mess by themselves. Regulators and mainline bankers failed to prevent smaller, highly leveraged financial institutions from building up huge pyramids of debt that forced them into ever more reckless practices. In a fascinating glimpse into the way Japan works, the accusations and cross-accusations are revealing a pattern of cooperation among MOF elites, politicians, banking executives, and the criminal gangs. This recognition is rocking Japan's political world, and it explains, in part, the surprise resignation on Jan. 5 of Socialist Prime Minister Tomiichi Murayama. After he announced the $6.8 billion taxpayer bailout on Dec. 19, his political position became untenable.

Successor Ryutaro Hashimoto, president of the Liberal Democratic Party, will feel the heat, too. In late January, the Japanese Diet will hold hearings on the MOF-brokered bailout of Japan's seven insolvent housing-loan corporations, or *jusen*, some of which are *yakuza*-linked. These *jusen* rang up $65 billion in dud loans on soured developments of everything from condominiums to golf courses.

As Finance Minister from 1989 to 1991, Hashimoto will need to explain why the *jusen* were exempted from rules aimed at curbing real estate lending—all the more so since taxpayers could be hit to the tune of $20 billion when the *jusen* bailout is finished, according to some estimates. Sensing blood, the opposition leader, New Frontier Party President Ichiro Ozawa, is attempting to exploit anger over the bailouts. "This is all being done under a veil," figures Ozawa.

To help with the cleanup, Japan plans to set up its own version of America's Resolution Trust Corp., with Japanese police backing. The cops would have the power to raid offices, grab records, and trace where *yakuza* money has gone.

But a true unmasking of the unholy alliance between the *yakuza* and the banking world would require an investigative campaign that would prove deeply embarrassing to business elites from Tokyo to Osaka. Also, there would be more than a certain measure of hypocrisy in an MOF-led campaign to portray the *yakuza* as the primary culprit in Japan's bad-debt mess, says Yukio Yamanouchi, a *yakuza* defense attorney in Osaka and former legal adviser to the 33,000-member Yamaguchi-gumi, the nation's biggest gang, led by Yoshinori Watanabe. "The bubble was the result of banks lending money too easily, while the government tolerated a policy of a high yen and a low U.S. dollar," Yamanouchi says. The gangs themselves never comment publicly.

What will future probes reveal? Police investigators, MOF officials, and *yakuza* sources point to several patterns of gang involvement with Japanese lenders. They center on roughly 24 real estate companies that Japan's National Police Agency has identified as having *yakuza* ties, if not outright ownership (table). They, in turn, borrowed money and later preyed on smaller lenders, such as the *jusen* and credit unions, that collectively became big players in Japan's go-go real estate market.

FOWL PLAY. Even when *yakuza*-affiliated institutions didn't actually own property, the gangs were instrumental in forcing rapid changes in ownership. At first, Asaji and other land turners didn't encounter much competition from established gangs in the land-extortion racket. Asaji would work discreetly with the real estate arms or other nonbank affiliates of local lenders. "During the bubble era, the banks set up subsidiaries and finance companies," he explains. "It was through these companies they would pay or loan to us," often in return for clearing property. Sometimes his methods were creative. Asaji once shipped in nearly 100 chickens to create a stench in a property next

THE PLAYERS

Most of the alleged yakuza-related lending was channeled through financial institutions such as these:

REAL ESTATE COMPANIES At least 24 of them lent heavily to gang-related real estate projects or rented out space to them. Now the companies can't pay back their loans to the banks because the gangs aren't repaying either.

JUSEN These housing-loan corporations, similar to U.S. savings and loans, were set up in the early 1970s, to supply credit to homeowners. But in the 1980s, they started lending to gang-linked real estate developers. Result: Some 50% of their $130 billion loan portfolio is underwater.

CREDIT COOPERATIVES Once primarily small-business lenders, the credit co-ops lent heavily for real estate. Some of the lenders have ties to the mob, according to officials.

AGRICULTURAL COOPERATIVES These rural institutions lent $52 billion to insolvent *jusen*. They are part of the politically powerful farm lobby, a big support base for the ruling Liberal Democratic Party.

SILK AND SINEW: *Gang leader Watanabe, arms crossed, at a shrine*

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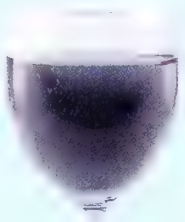

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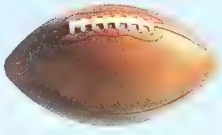

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to a house to persuade—successfully—an owner to sell.

But by the late '80s, as property prices surged monthly, *yakuza* outfits started moving in on his turf and were even hired by his extortion targets. "They started bringing in *yakuza* to counter independent operators like me," Asaji said. "I hated paying the gangs, so I had to hire a higher-grade *yakuza*, like Yamaguchi-gumi, to survive."

Over time, the Osaka gangs cemented their ties with lenders and real estate companies to a startling degree. Last year, when Osaka regulators started scrutinizing the books of busted regional credit union Gifu Shogin, they found that nearly $70 million in loans were linked to *yakuza*-related real estate companies, according to a source with Kansai Kogin, the entity that absorbed the busted lender. The loans had gone into condo and office development. When property prices crashed, Gifu started to call in the loans, but the *yakuza* wouldn't pay and grew threatening. Bank managers had to bring in police for protection.

RATE BAIT. Perhaps the biggest bombshell to come, though, will be Osaka-based Kizu Credit Cooperative, a $12.3 billion thrift, formerly Japan's largest, that collapsed in August after a massive deposit run. A ferocious land speculator with $9.1 billion in dud loans, Kizu is one of the most expensive bank failures to date, having already drained more than $1 billion in Bank of Japan money to cover deposits. It likely will be the target of a criminal investigation because of suspected loans to "dubious companies," says one Ministry source.

Under the leadership of Kizu President Minoru Kagiya, the thrift diversified away from business lending into real estate. And to build a war chest, it started luring depositors with interest rates as high as 2% above the market. From 1987 to 1990, one of its biggest sources of funding came courtesy of Sanwa Bank Ltd., the Tokyo money-center giant.

Sanwa arranged for its corporate clients to raise millions in short-term commercial paper. The clients would then deposit the money into Kizu and benefit from the big spread between their high-interest thrift account and what they were paying on their corporate IOU. It seemed to be a risk-free way of locking in profits. Sanwa, meanwhile, profited handsomely from its underwriting fees.

> Loans became more and more reckless as banks tried to survive on interest income

By 1989, some 36%, or about $3 billion, in Kizu deposits came from Sanwa, and about 10 of its ex-employees were working for Kizu, Osaka regulators say. A spokesman for Sanwa confirmed that his bank dealt with Kizu but said the practice ended in 1990. He stressed that the bank has no knowledge of possible Kizu ties to the mob. The blue-chip Long Term Credit Bank of Japan also steered money, though smaller amounts, to Kizu, but severed relations in 1991, a spokesman says.

What did Kizu do with its deposit windfall? Investigators suspect some of the money went right into the pockets of *yakuza* gangs, sometimes for clearing land and in other instances for loans. According to Asaji, Kizu and its two affiliated companies steered direct loans to the land turners or the property developers who used them. Kizu declined to comment.

After reviewing Kizu's books, Osaka regulators say they have evidence the thrift intentionally inflated the value of its loans on Osaka-area properties. When property prices skyrocketed, Asaji says Kizu would lend more than the market value of a project to factor in the costs of using the land turners, called *jiageya*. "Even if they knew the money would go toward *jiageya*, they would still lend," Asaji says.

CRISP NEW BILLS. When land values collapsed, starting in 1991, an increasingly desperate Kizu continued the practice to keep its interest income high. "If they knew a property was worth $5 million, they would provide a $10 million loan to inflate interest income, even if they knew the loan would never be repaid," explains Shigenobu Suzuki, an Osaka credit union regulator.

After Sanwa and others severed relations and property prices fell, Kizu started offering suicidal deposit interest rates and made one reckless loan after another in a desperate bid to keep

KIZU: A TRAIL OF MONEY

BUREAUCRATS The Ministry of Finance and the Bank of Japan created loose credit policies in the late 1980s, which helped property prices skyrocket and encouraged a flood of real estate speculation.

SANWA BANK ▶ It persuaded corporate clients to borrow at cheap commercial rates and redeposit the money at Kizu Credit Cooperative, which offered above-market interest rates. Companies benefited from the spread, and Sanwa enjoyed big underwriting fees on the commercial paper.

KIZU The Osaka institution used its inflated deposit money to increase its loan volume to real estate lenders, who poured money into everything from golf courses to apartment developments.

JIAGEYA Kizu's borrowers, flush with easy money, hired *yakuza*-related groups to evict renters or scare reluctant sellers. One self-acknowledged *jiageya* was Hiroshi Asaji, in Osaka, who intimidated owners.

◀ **COLLAPSE** When property prices crashed, Kizu went bust and depositors panicked.

DATA BUSINESS WEEK

its income high enough to fund operations. By the time its money-churning strategy crashed in August, some 88% of its loan portfolio had been steered into dud property deals on behalf of 10 real estate companies, at least some of which had *yakuza* ties, investigators say. To add insult to injury, Osaka police still are trying to track down who walked off with $1 million worth of neatly pressed yen notes from Kizu headquarters that the Bank of Japan provided during the deposit run.

As the MOF tries to get serious about cleaning up the mess, it is stumbling into dozens of examples of mob involvement where the trail ultimately leads to money-center banks. Regulators barred these banks from taking direct part in the dirty-money games of the late 1980s. But they winked when the banks began using affiliated finance and real estate companies such as Kizu to go for quick, big returns in deals that often involved the *yakuza*. "That way, [the bankers] could say, 'Hey, it's not on my books,'" says J. Brian Waterhouse, banking analyst for James Capel Pacific Ltd. "When money begot more money, unsavory characters were sometimes allowed to move in."

TALL ORDER. As shocking as the extensive *yakuza* involvement may be, there is scant prospect that regulators will be able to fundamentally reorder the financial system. Going after the *yakuza* will be a tall order unless the financial executives who hired them or financed them also take the fall. Until they do, the image of a Japan unable to clean house, bolstered last year by bank runs and the $1.1 billion Daiwa Bank Ltd. treasury-bond trading scandal, won't vanish any time soon. Nor will the "Japan premium" that has driven up the interest rates that Japanese banks must pay to borrow internationally.

None of this means that Japan as a whole is somehow doomed. Its industrial economy has been largely untouched by the *yakuza*-related scandals, and, indeed, seems about to recover. What it does mean is that political leaders, financial authorities, and bankers are likely to be bogged down in coming months and years, trying to find a way to clean up the bad loans without going so far that they reveal their entire system was tainted by corrupt dealings. Chances are slim that much money will be recovered from the gangs. "Even if they crack down on the *yakuza*, it doesn't mean they will get the money," says gang attorney Yamanouchi. The reason is that the gangs and their associates, such as Asaji, possess a powerful weapon: the knowledge that they did not act alone.

By Brian Bremner in Osaka

THE SAMURAI MEETS THE GODFATHER

The ties that bind Japan's *yakuza* to banks and real estate companies are scarcely a surprise to Japanese in the Kansai region, which encompasses Osaka, Kobe, and Kyoto. The headquarters of Japan's biggest gang, the Yamaguchi-gumi, is located in a posh residential neighborhood in Kobe and has become something of a landmark. The gang even won kudos for pitching in with food and supplies after last year's earthquake in Kobe, which killed more than 6,000 people.

NOVELIST YAMANOUCHI: *Lonely, mixed-up hit men*

Nor was it much of a shock when *yakuza* representatives showed up at a fund-raiser for Osaka Governor Isamu Yamada last summer at the swank Royal Hotel. Unlike Western countries, where gangs keep a low profile, the *yakuza* have long been an accepted part of the system in Japan. Members are glamorized as misunderstood social outcasts and guardians of Samurai notions of honor.

CULT FIGURES. Throughout Japan's postwar history, political and business elites have turned to the gangs in time of need. During the 1960s, ruling Liberal Democratic Party governments used the *yakuza* to put down radical left-wing labor and student protests. And until recently, the government tolerated some company's use of gangsters called *sokaiya* to keep unruly investors in check at annual meetings. "In a dysfunctional political system like Japan's, the *yakuza* thrive," muses Raisuke Miyawaki, a former *yakuza* investigator who now advises companies on how to respond to gang threats.

Changing their image won't be easy, given the sentimental treatment of *yakuza* characters in popular culture. These are men who sometimes cover themselves with tattoos and are willing to have finger joints ritually amputated as a token of loyalty. Osaka attorney Yukio Yamanouchi, a former legal adviser to the Yamaguchi gang, earns $200,000 annually cranking out breathtaking *yakuza* tales. His best-selling novel, *Kanashiki Hittoman*, or *Lonely Hit Man*, even became a smash-hit film in 1989. Yamanouchi and others have generated public sympathy by portraying the *yakuza* as a haven for *burakumin*, the untouchables, members of the lowest caste of Japanese society.

Maybe so, but Japanese police authorities have trouble feeling sorry for the *yakuza*. In addition to traditional rackets such as gambling and prostitution, the gangs are the force behind Japan's growing drug trade and gun-running operations that contribute to violent crimes. And though an antiracketeering law in 1992 has reduced the overall number of *yakuza*, power has since been concentrated in the hands of the three major outfits: the Yamaguchi-gumi in Kobe and the Inagawa-kai and Sumiyoshi-kai in the Tokyo area.

Now that the Ministry of Finance and Japan's new Prime Minister, Ryutaro Hashimoto, have pledged to drive the *yakuza* from the banking world, the public may see a less romantic view of the gangsters—namely, as extortionists who have contributed to Japan's economic slump. Says National Police Agency investigator Takafumi Shimoda: "The *yakuza* have been romanticized by the public, but they are really social parasites." Until that becomes the consensus view, however, count on the *yakuza* to continue swaggering in public view.

By Brian Bremner in Osaka

NEW ANGLE: *Workers at OWP Brillen may cut a deal to save jobs*

GERMANY

ARE THE EASY TIMES GONE FOR GOOD?

Germany has a giant jobs crisis that threatens its labor peace

On a foggy morning in January, five employees taking a coffee break at a railcar factory in Siegen, Germany, talk gloomily about work. For the past three years, they've watched hundreds of colleagues collect their last paychecks as their employer, ABB Henschel, started making railcars at low-cost sites in Poland and the Czech Republic. They know something is wrong with a Germany that now exports its jobs instead of creating more at home. "The whole system has to be fixed for our children and grandchildren," laments Werner Schulz, 54, an accountant. Agrees Ulrich Kromback, a 45-year-old welder in blue coveralls: "It's more urgent than ever."

From the shop floor to the Chancellor's office, the realization is finally sinking in: Germany has a giant job crisis. Unions and employers tried over the past few years to ignore this fact and instead kept ratcheting up wages and benefits until German labor costs became the highest in the world. But now, German unemployment, at 10%, is at a postwar high and shows no signs of declining. The economy seems incapable of creating new jobs, and labor negotiators and employers are desperately trying to figure out a course of action. "We've talked enough—now we've got to do something," admits Julius Louven, a labor expert in the Bundestag. That "something" could lead to a dramatic revision of Germany's prized social contract.

GOING ABROAD. On Jan. 23, Chancellor Helmut Kohl and his advisers will sit down with union and employer representatives to discuss the best way to revive business activity and get Germans working again. All three groups are under mounting pressure to produce. Unions want to reverse their dwindling membership rolls, down 20% in four years. Employers are still red-faced at being duped into a very expensive deal in 1995 and would dearly like to cut wages and benefits. And Kohl, mindful of his narrow majority, wants to use the jobs issue to boost his party's image ahead of local elections in March.

Already, Klaus Zwickel, chief of the powerful metalworkers union IG Metall, has upstaged everyone else. He is proposing an Alliance for Jobs, in which employers promise to create 330,000 jobs starting this year, unions hold back their wage demands for 1997, and Bonn forgoes planned cuts in long-term unemployment pay.

The employers are glad that Zwickel finally recognizes the need for wage restraint if German jobs are not to disappear en masse. But the call for a guaranteed boost in employment alarms players in the financial markets. "[Zwickel] is calling for central planning," scoffs Thomas Mayer, chief economist at Goldman, Sachs & Co. in Frankfurt. "Germany needs market-based solutions to reflect the competitive environment."

Countering Zwickel's vision, business wants flexibility in the labor market, tax breaks, spending cuts, and deregulation in the economy overall. In mid-January, in a clear retort to the Zwickel manifesto, Hans-Olaf Henkel, head of the Federation of German Industry,

THE GERMAN DILEMMA

COSTLY LABOR

Average wages and benefits for a manufacturing worker are $30 an hour

SLOW ECONOMY

GDP grew only 1.9% in 1995 and may hit only 1% this year

UNEMPLOYMENT

The rate of joblessness is approaching 10% with no improvement in sight

DATA: OECD, BUSINESS WEEK, DRI/McGRAW-HILL

ublished an eight-point plan sounding ll these themes. Among other things, Henkel calls for a cut in social levies, to 7% of income from 41%; specific tax reaks to encourage employment; and a greater role in wage negotiations for ocal workers, who presumably know heir employers better than national nions. Henkel argues that this way, 2 nillion jobs could be created by 2000.

Undaunted, other unions are talking bout job-creation schemes and are trongly hinting that strikes could break ut unless Zwickel's plan becomes the lueprint for generating jobs in Germa-y. Yet the employers, for now, are not eady to compromise. Nothing is stop-ing them from investing abroad, where abor is cheaper and skilled workers are asy to find. German companies such as Siemens and BMW continue investing in locations as diverse as Poland, Malaysia, and North Carolina. Bayer, which is rapidly expanding in China and south-east Asia, cut its German payroll by over 4,000 in 1995. Says CEO Manfred Schneider: "We cannot create any new jobs in Germany."

***MITTELSTAND* ANGST.** Employers also feel they have been generous enough—too generous—with German labor. In early 1995, when it looked as if the economy would grow by 3%, IG Metall secured a deal that, including shorter hours and lower-than-expected inflation, pushed wage costs up by more than 10% as of December, 1995. In eastern Germany, the 1995 pact—coupled with the plan to bring wages up to levels in western Germany—boosted pay costs by more than 20%, a sum midsize employers cannot afford.

Those high-cost deals are driving many members of Germany's vital midsize corporate sector—the *Mittelstand*—to seek their own solutions with labor. Berthold Dentler is president of OWP Brillen, a maker of high-fashion eyeglasses in Passau with $25 million in annual sales. The recent wage deals cut by IG Metall and Gesamtmetall, the employers group, boosted expenses so fast that his company sank into the red in 1995. Disgusted, he quit Gesamtmetall in September and offered his employees his own pact: a deal involving a longer workweek, profit-sharing, and, Dentler hopes, a chance to save jobs.

Dentler's employees will vote on his proposal at the end of the month. Whatever their answer, Dentler feels the easy times are gone for good. "Germany needs to see things the way they are, not as we wish them to be," he says. This is the year when Germans may really start grappling with their country's new realities.

By Karen Lowry Miller in Passau, Germany

KUWAIT LOOKS AT ITS SOUL—AND ISN'T HAPPY

Has the welfare state destroyed the competitive spirit?

As a scion of Kuwait's ruling family, Sheikh Nasser Sabah Al-Ahmad Al-Sabah has the means to do just about anything he wants. He seems very comfortable enjoying the evening air at a modest beach house on Kuwait's coast. There, he likes to dine informally on grilled fish, fresh from a trap out in front, with a small group of companions and retainers.

In the 1970s and 1980s, Sheikh Nasser, now 48, built a magnificent collection of Islamic art and put it under the auspices of the national museum, which was later looted by the Iraqis. Now, he has a more ambitious goal: helping define a new national agenda. He worries that decades of living passively off oil revenues have turned Kuwait—originally a nation of tough, resourceful traders—into a soft "welfare society." He warns that Kuwait—whose very existence was almost snuffed out five years ago by the Iraqis—won't have much of a future unless its people relearn the value of work and the reality of competition. "Our whole history is based on a free-market economy," he says. "Then, with oil, we felt we didn't need tough competition."

SHEIKH SAAD: *Pressure for reform comes from a fractious parliament*

Sheikh Nasser is one of many influential Kuwaitis who are debating their country's future. He has started a magazine, *Al-Zaman*, as a forum for new thinking. Such soul-searching is occurring throughout the region, but in Kuwait, discussions are far more open and vigorous, thanks to a largely unfettered press and a freewheeling parliament. Among the big issues are government corruption and a yawning budget deficit that supposedly threatens the funds set aside for future generations.

Some Kuwaitis say that the Iraqi invasion—catastrophic as it was—gave the emirate a rare chance to reshape its policies, control spending, slash reliance on foreign labor, and revitalize the private sector. After regaining their country, the people were ready for sacrifice and tough reforms, argues economic consultant Jasem K. Al-Sadoun. Instead, the government headed by Crown Prince and Prime Minister Sheikh Saad Al-Abdullah Al-Sabah is following the paternalistic model by boosting handouts and preserving a

statist, protected economy. "The incompetence of management has almost led us to lose the opportunity to reconstruct our policies," Al-Sadoun says. Sheikh Nasser's magazine recently featured Al-Sadoun's views in a long interview. The magazine and a recent symposium sponsored by Sheikh Nasser have drawn a good deal of interest locally because they seem like an intellectual challenge to the leadership from inside the family.

Some of the government's toughest critics are in parliament, which relishes the role of financial watchdog and advocate for the ordinary citizen. It is a thorn in the side of the leadership but also a useful safety valve. "We need a very radical restructuring," says Abdalla M. Al-Nibari, a member of the National Assembly's finance committee. "We have been limiting our capital expenditures. In a few years' time there won't even be enough for maintenance."

PLENTY OF CASH, BUT: *Kuwait's 1995 deficit equaled 35% of GDP*

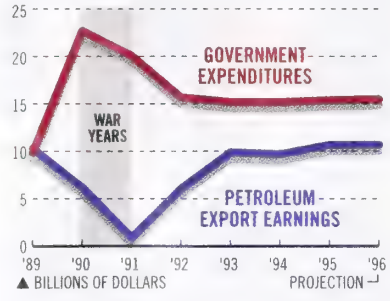
BIG GAP. The budget deficit is as big an issue in Kuwait as in the U.S. The government has run deficits of $5 billion to $6 billion per year since the gulf war. In 1995, the deficit was about 35% of gross domestic product. The big worry is that the government is depleting its financial reserves. Sharif Ghalib, senior vice-president and chief economist of Kuwait-based Gulf Investment Corp., estimates that the foreign assets fell from $100 billion before the war to about $55 billion today. He thinks they are now increasing modestly.

Still, Kuwait is spending billions in investment income, and that disturbs the man in charge of the country's overseas portfolio. The budget deficit "could be affecting our operations," says Ali A. Rashaid Al-Bader, managing director of the Kuwait Investment Authority. "The investment portfolio is for future generations when the oil is used up—not to pay the expenses of the state."

But there is no doubt about Kuwait's solvency. Some of this hand-wringing may be intended to make reform easier and to deflect requests from the U.S. and other countries for Kuwaiti money for such projects as a development bank to support Middle East peace. Indeed, the government has begun paying down the $5.5 billion loan that J.P. Morgan & Co. arranged for war expenses. And Al-Bader says the government may go into the markets for more money.

Al-Bader is under a lot of pressure. Since taking over the KIA after the war, he has had to pursue court cases against former officials accused of bilking Kuwait's investment funds of billions of dollars in scams in Spain and elsewhere. He has also been the point man for controversial privatization moves. Feeling harassed, he recently submitted his resignation but was persuaded to stay.

KUWAIT'S SPENDING TOPS ITS OIL INCOME



DATA: PETROLEUM FINANCE CO.

Al-Bader says the government is mulling steps to close the deficit. These may include raising prices on gasoline and on highly subsidized services such as electric power and local telephones. The government is also preparing sell-offs of some of the state monopolies. Al-Bader says telecommunications is likely to be the first to go. The plan is for an international phone company to take a 25% stake. Kuwait Airways Corp. may also be privatized.

But none of this will be easy. Almost any initiative that would raise prices for Kuwaitis or cost them jobs provokes an outcry in the press and parliament. Any effort to boost taxes or fees on ordinary Kuwaitis will be attacked, not least because the government assumed some $20 billion in bad debts of stock speculators and other fat cats in recent years. Most observers think Sheikh Saad will proceed very warily—at least until after next fall's parliamentary elections. "Because you have an open society and a fractious one, things tend toward stasis," says a Western diplomat.

Indeed, the status quo is very comfortable for Kuwaitis. They enjoy a cradle-to-grave welfare system that provides nearly all of them with government jobs and free education and health care. The government and its affiliates account for 85% of the local economy and employ 93% of the 166,000 Kuwait labor force. Only 9,500 Kuwaitis work in the private sector. A 25% salary increase handed out to Kuwaiti public sector employees after liberation served to discourage private-sector work. "They have almost convinced the people that working for the private sector is nonsense," says Al-Sadoun. Official statistics show that foreign residents now outnumber Kuwaitis by 1.1 million to 695,000.

A FIRST. Kuwait is likely to whittle away at the public sector. This should provide opportunities for foreign companies as the government seeks outside expertise and capital. Last July, Union Carbide Corp. and Kuwait's Petrochemical Industries Co. broke ground on a $2 billion joint-venture petrochemical plant—the first major foreign investment permitted in Kuwait's oil sector.

Sales of companies the government bought while bailing out stock speculators in the 1970s and 1980s are also giving the private sector a bigger role. Such sales generated $1 billion in revenues last year and could produce a further $2.5 billion. "The government may not be improving, but the receptiveness to change is increasing," says Tarek A. Sultan, managing director of New York Associates, a local investment bank.

But real change will be very tough. Some influential Kuwaitis, and even a portion of the royal family, are dissatisfied with the status quo. Whether they can push the country to make major reforms is another question.

By Stanley Reed in Kuwait City

EDITED BY STANLEY REED

WHY CHINA'S NERVOUS LEADERS ARE CRACKING THE WHIP

In the interior Chinese city of Xian, it is now routine for squads of soldiers to show up at local elementary schools. They assemble the students and drill them in marching and other military skills, while leading them in praise of the Communist Party and the 3.2-million-strong People's Liberation Army. Such indoctrination sessions, which were rare until recently, sometimes last as long as 10 consecutive days.

The raised profile of the PLA in China's provinces is just one sign of a tougher line by Beijing on everything from domestic dissent to religion to foreign trade. The latest indication of this trend was the Jan. 16 announcement that within the next three months, such providers of electronic financial information as Dow Jones, Reuters, and Bloomberg would have to have their products distributed and screened by the official Chinese news agency, Xinhua. In announcing this big shift, Xinhua said the government will punish companies that release reports that contain information "forbidden by Chinese laws or that] slanders or jeopardizes the national interests of China."

TOP DOGS. While this move is undoubtedly partly motivated by Xinhua's complaints that its business was threatened by foreign competitors, the step is a sign of the insecurity of China's leaders as 91-year-old Deng Xiaoping fades from the scene. When healthy, Deng was strong enough to do just about anything he wanted. But hand-picked successor President Jiang Zemin feels he has to pay court to the increasingly influential hard-liners. China's top dogs are growing worried that the last four years of freewheeling growth have taken too much power away from the central government. They are scrambling to regain control through pandering to the military, cracking down on dissent, and strengthening macroeconomic restrictions.

PAYING COURT
President Jiang Zemin feels he has to mollify influential hard-liners, so the People's Liberation Army is getting more and more of what it wants

Not just foreign news agencies but Western investors that have plunked down billions in China in recent years could start feeling the chill winds of China's new conservatism. Fearful that multinationals are grabbing too much market share in key industries, the resurgent State Planning Commission is preparing tough industrial policies that would restrict foreign equity and require greater technology transfer and exports in sectors ranging from consumer electronics and telecommunications equipment to automated machine tools.

China's ambitions to join the fledgling World Trade Organization could also be sacrificed. Even though Beijing is slashing import tariffs and insists it wants to join the WTO immediately, China is making other moves that suggest it's willing to push back that goal indefinitely. One reason may be that Washington is setting very tough conditions for China's membership. "China's leaders have decided the price of joining the WTO is just too high," says Nicholas Lardy, a specialist on China's economy at the Brookings Institution in Washington. "Opening up sectors as rapidly as the West has demanded would hurt the state-owned industries too much."

It is not yet clear how tight the controls on financial information will be. So far, Xinhua hasn't released many details. A lobbying campaign by international media and domestic financial institutions could persuade Beijing to water them down. The Xinhua power play has local companies complaining as well as foreign ones. "We're very concerned about whether we will still be able to get information freely and in a timely fashion," says a Beijing securities official.

But Beijing officials now seem willing to take the risk of stunting their financial markets' development. China's tone is very different from what it was a few years ago, when Deng gave his blessing to a huge shift to freer markets. Recently a Chinese-backed Hong Kong paper went so far as to run a story blasting the policy of high-speed growth in the coastal provinces during the early 1990s as "crazy."

The shift toward conservatism doesn't seem likely to stop anytime soon. It is being accompanied by a marked growth in military influence. The generals are getting a bigger slice of the budget than before and have certainly contributed to Beijing's tougher approach—especially on the Taiwan issue. The military also seems increasingly suspicious of Washington. It believes the U.S. is pursuing a policy of containing China. PLA leaders frequently use the cold-war phrase "hegemonism" when criticizing American actions. The military doesn't mind Jiang's slowing down reforms or harping on "social stability." After all, a government that emphasizes military virtues such as patriotism and order is bound to give the PLA much of what it wants.

But the big question is what sort of toll this conservatism is going to take on the economy. At the moment, the hard-liners have the reformers on the defensive, but one wonders what will happen if China's markets start tanking or investment flows drop. Should influential Chinese start to suffer, the winds could shift again.

By Joyce Barnathan and Pete Engardio in Hong Kong, with Dexter Roberts in Beijing and Dave Lindorff in Xian

SOCCER

IS MAJOR LEAGUE SOCCER USING ITS HEAD?

Its structure may avoid problems plaguing other sports

Sure, Americans like an underdog. But Alan I. Rothenberg, a fast-talking Los Angeles lawyer, is peddling a product that the public has rejected time and time again over the past 30 years: pro soccer.

Reared on baseball, enthralled by basketball, and steeped in the traditions of football, U.S. sports junkies have long yawned at the low-scoring game that the rest of the world loves. So Rothenberg, chairman of Major League Soccer, due to debut this spring, is counting on soccer's popularity among kids and Latinos to pull in fans. And, he says, the league's unique financial structure will help it avoid the lawsuits, sudden franchise moves, and whiny millionaire players plaguing other pro sports. "The timing is better than it's ever been for professional soccer to succeed," says Rothenberg.

LATE KICKOFF. Maybe. But there have already been stumbles. For starters, poor organization and a cool response from sponsors delayed the league's kickoff by two years. The result: Instead of starting just after the successful 1994 World Cup, hosted by the U.S., and during the baseball strike, MLS's inaugural season will compete with the national pastime and the Atlanta Olympics. "We just weren't ready," says Rothenberg, who ran the World Cup.

If pro soccer has any chance this time around, it will need to avoid the mistakes of past attempts, especially those of the North American Soccer League, which died in 1985. Like most sports leagues, it allowed investors to own their own teams. That led to big disparities in capital. While Steve Ross, then CEO of Warner Communications, signed stars such as Pelé to his New York Cosmos and drew throngs, small-market clubs struggled.

MLS's solution: Structure the league as a single entity so that investors will operate—but won't own—the teams. Instead, they'll be partners in one enterprise. The more revenue a team brings in, the better the return its operator will get—but a low salary cap will preserve parity. The setup should sidestep the lawsuits between teams and leagues common elsewhere in pro sports, says National Basketball Assn. Commissioner David J. Stern.

So far, MLS has reeled in some big-fish investors, including New York billionaire John W. Kluge, self-made oilman Phillip F. Anschutz, and Lamar and Clark Hunt of the Texas oil family. Billionaire hedge-fund investor George Soros joined a group that will operate the Washington (D.C.) team. The question is whether those investors will be satisfied with holding only partial control, especially if the league grows. "It can work—as long as you keep the egos in check," says Gordon Kane, senior vice-president at Clarion Performance Properties, a marketing firm.

The league has also attracted some brand-name advertisers. AT&T, Anheuser-Busch, Kellogg, and Nike are each paying up to $2 million a year for sponsorship rights. A Fuji deal will be announced soon. Add to the mix a pact with ESPN that puts 35 games on the air this year, and MLS is guaranteed far more exposure than its predecessor.

To help build a U.S. market, MLS has also made a commitment to promoting U.S.-born players. Alexi Lalas, the red-haired dervish who led the U.S. to a stunning upset of Colombia in the World Cup, will play for the New England Revolution, and his face will grace a box of Kellogg's cereal later this year. That's a direct appeal to the 13 million soccer-playing kids in the U.S.

The other core fan base will be Latinos, who follow foreign teams on Spanish-language television. But winning over these knowledgeable fans will take more than savvy marketing. So the league has signed international stars such as Mexican national goalie Jorge Campos. He will play for the Galaxy in Los Angeles—a clear attempt to woo the city's Mexican-Americans.

Still, there are no guarantees the MLS can meet its goal of about 12,000 fans a game. Tens of thousands may have turned out for the World Cup's pageantry, but that doesn't mean they'll show up for a Tuesday night match between the Columbus Crew and Kansas City Wiz when they could be home watching the basketball playoffs. If Rothenberg and new MLS Commissioner Doug Logan can't sell games like that one, pro soccer could end up where it's been before: face down in the dirt.

By David Leonhardt in New York

TRYING OUT: *Drawing fans will be the tough part*

A League of Their Own

Team	Investor/Operator
NEW ENGLAND REVOLUTION	ROBERT KRAFT
COLUMBUS (OHIO) CREW	LAMAR AND CLARK HUNT
DALLAS BURN	LEAGUE-RUN
COLORADO RAPIDS	PHILLIP ANSCHUTZ
KANSAS CITY WIZ	LAMAR AND CLARK HUNT
LOS ANGELES GALAXY	GROUP OF LOCAL INVESTORS
NEW YORK/NEW JERSEY METROSTARS	JOHN KLUGE AND STUART SUBOTNICK
SAN JOSE CLASH	LEAGUE-RUN
TAMPA BAY MUTINY	LEAGUE-RUN
D.C. UNITED	GROUP INCLUDING GEORGE SOROS

DATA: MAJOR LEAGUE SOCCER

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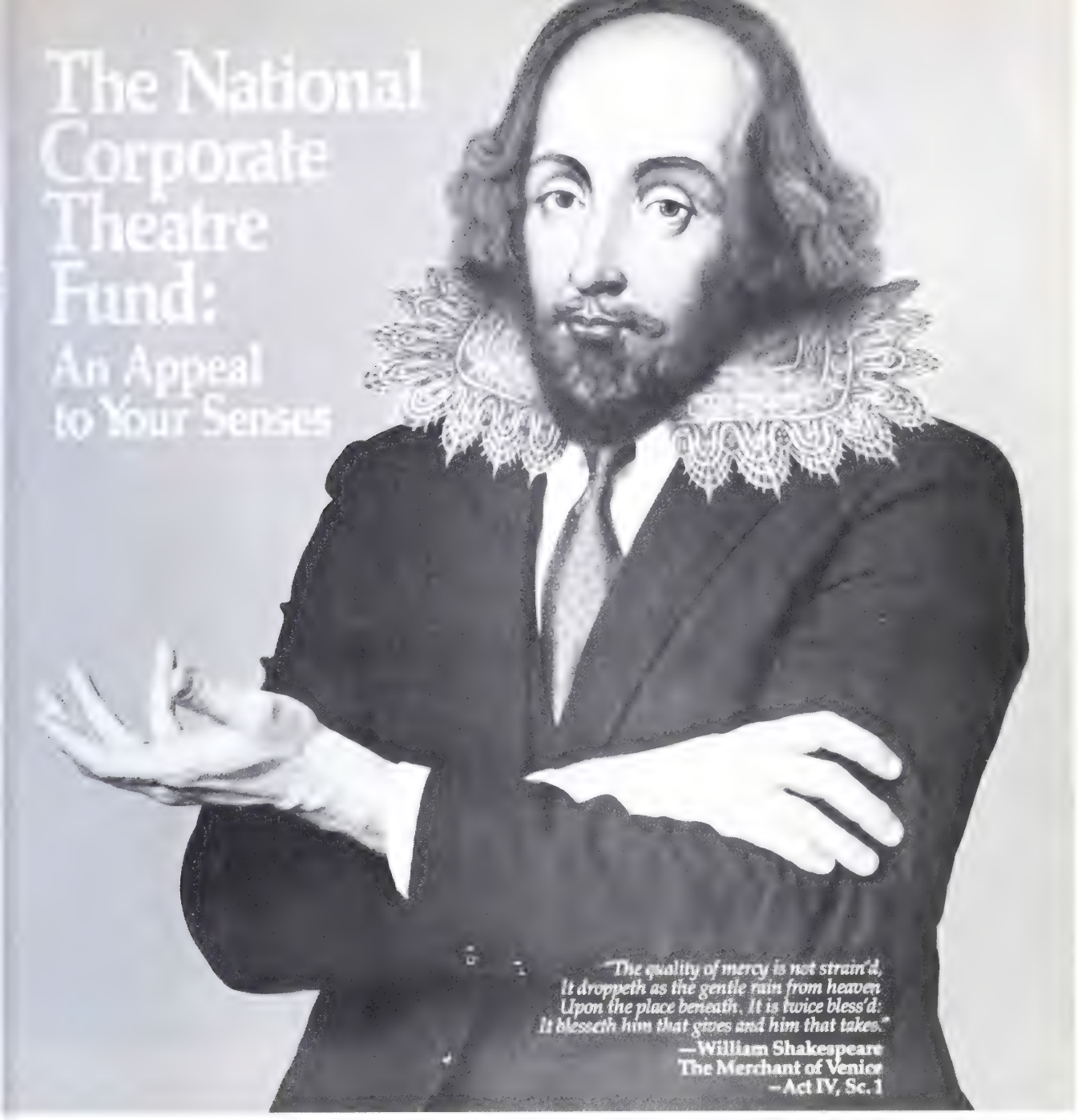
An Appeal to Your Senses



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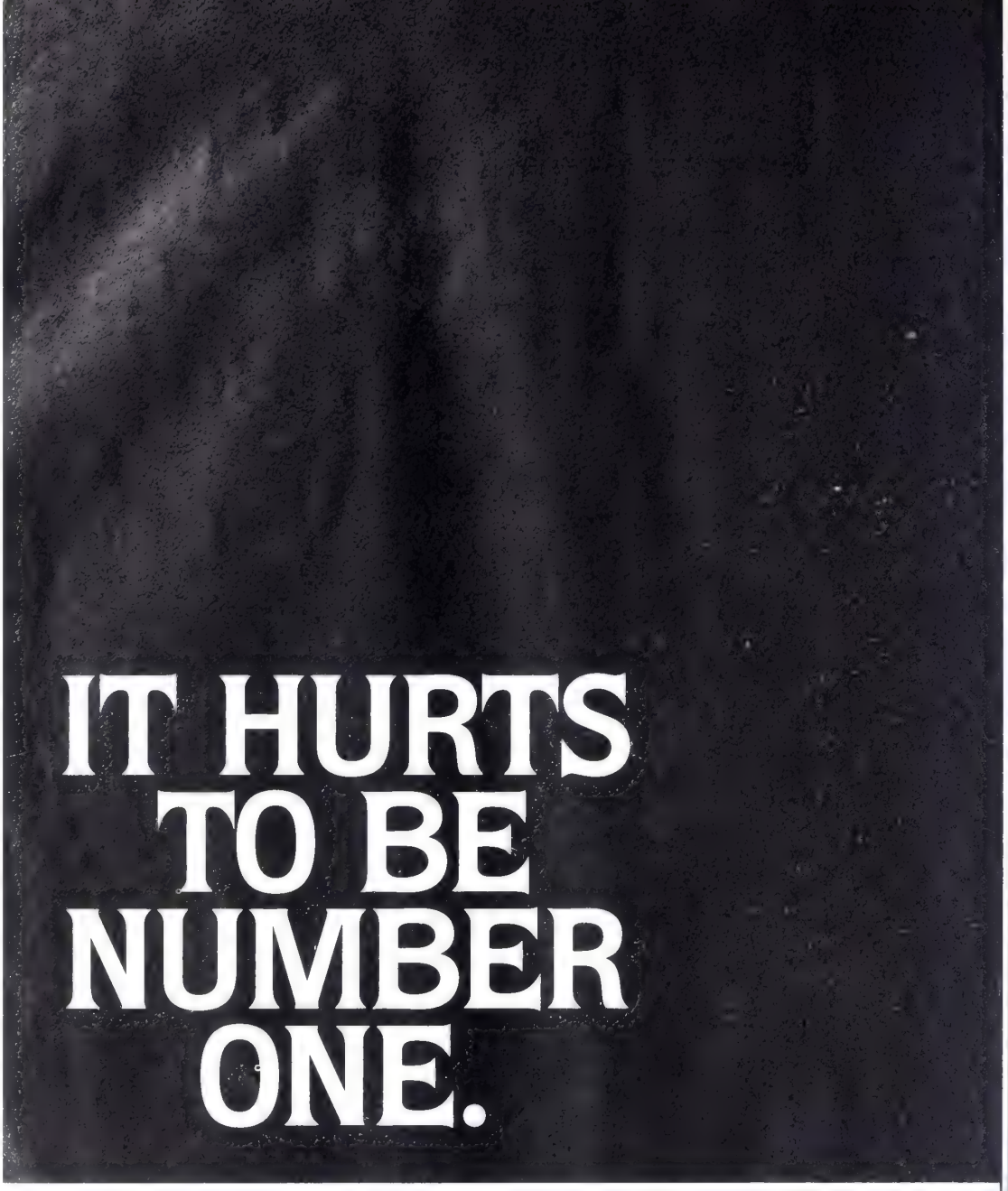

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SPONSORSHIPS

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Corporations aren't just slapping logos on arena marquees

It's the latest corporate fad. With new stadiums going up faster than quarterbacks' salaries, Corporate America is rushing at a record pace to slap its logos on them. From Nynex Arena in Manchester, England, where the phone company owns cable properties, to GM Place in Vancouver, the rights to arena names now belong to the highest bidder. Even Boston Garden has given way to Fleet Center, courtesy of a Fleet Bank sponsorship.

Why the sports craze? Because for just $1 million or so a year, marketers can buy the chance to reach tens of thousands of consumers at every sports event and concert held, week in and week out. That looks pretty good next to alternatives such as 30 seconds on *Seinfeld* for $400,000 or a half-minute on the Super Bowl for $1.2 million. Besides, if the hometown team makes it to a championship, marketers can get a national TV audience at no additional cost.

FREEBIES. "Companies are always looking to increase their public exposure, and this is a pretty good way to do it," says Timothy Orchard, a vice-president at stadium manager Ogden Entertainment Services. "The number of impressions is almost unlimited." The free tickets to spread among customers and employees and the chance to show good corporate citizenship don't hurt, either.

Corporations have had their names on stadiums in the past, of course. Anheuser-Busch Cos. owned the St. Louis Cardinals and the arena they play in—Busch Stadium—for more than 40 years before agreeing to sell both last month. But now, there's an explosion of new opportunities, thanks to a boom in stadium-building and renovation. Team owners and cities, pressed to attract fans in the face of mounting competition, have pushed for fancy new digs to house their teams, complete with executive suites that can pull in big profits. The new Fleet Center, for example, will have 104 suites that go for $200,000 annually. That's $20.8 million, split between the team and the center's owners.

The new sponsors are far from shy about exploiting their deals. GM is showing off its new line of cars at GM Place and has set up kiosks that answer product questions. MCI Communications Corp. is planning to wire up its Washington arena with all manner of high-tech communications gadgetry, including video screens at every seat. Fans will be able to watch the hockey action from the point of view of the players, who will have tiny video cameras mounted on their helmets. And 3Com Corp., which now has its name on the old Candlestick Park in San Francisco, has installed eight "Internet Spoken Here" video kiosks equipped with its networking software. Fans can use them to cruise through cyberspace between innings.

Such deals are not without their headaches. New Jersey's Brendan Byrne Arena announced a name change to Continental Airlines Arena just weeks ago and has already being sued by the National Basketball Assn., which claims its right to sell ad space was infringed upon. Last summer, Canadian Airlines International Ltd., which was in the middle of slashing expenses by $125 million, was blasted by the International Association of Machinists after it announced a $400,000-a-year deal over 20 years to put its name on Calgary's Olympic Saddledome. Says union President David Park: "That money should have gone to buying new airplanes." Meanwhile, when 3Com put its name on legendary Candlestick Park, apoplectic fans derided the change as an example of gross commercialism.

THE TAX CARD. That kind of reaction has companies treading carefully. A group of corporations interested in the naming rights to the new Boston Garden commissioned a survey to gauge public sentiment before submitting bids. A fifth of those polled opposed a corporate name for the new arena but softened after learning that the alternative was higher taxes and higher ticket prices. In the end, Shawmut Bank won with a $2 million-a-year, 15-year bid, but then handed the rights to Fleet when it was acquired by Shawmut in March, 1995.

As the lines between business and civic enterprises blur, corporate logos could encroach further. The Walt Disney Co., whose Mighty Ducks hockey team is already named after a Disney movie, made a pitch to put its logo right on the team uniforms, but the National Hockey League nixed the plan. Disney, which didn't want its name on a stadium that could host less-than-wholesome rock concerts, sold the stadium naming rights to a bottled-water company. But why stop at sports arenas? What about the Random House Public Library of the Ronald McDonald Municipal Airport?

By Mark Lewyn in Washington

Stadium Name Game

	LOCATION	SPONSORSHIP TERMS
PEPSI CENTER	Denver	$50 million-plus over 20 years
3COM PARK	San Francisco	$4 million over 4 years
AIR CANADA CENTER	Toronto	$14 million over 20 years
TRANS WORLD DOME	St. Louis	$26 million over 20 years
GM PLACE	Vancouver	$20 million over 20 years

DATA: BUSINESS WEEK, IEG SPONSORSHIP REPORT

OMINOUS SIGN? *Fans cried foul at Candlestick Park's renaming*

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INVESTIGATIONS

DID THE FAA GO EASY ON BOEING?

To O.K. the 777 jumbo on time, the agency downplayed a possible flaw, some engineers say

PRESSURE POINT: *Fan blades on the 777's huge twin engines are extra heavy. If a blade broke in flight, some say it could destabilize the plane*

Since June, Boeing Co.'s newest jumbo jet, the 777, has been logging daily flights between Washington and London. With its sophisticated new design—drawn up entirely on a computer screen—the $4 billion aircraft program is a technological and commercial triumph for the nation's largest plane manufacturer. The $4 billion Malaysia Airlines order last week that included 15 of the new planes confirmed what many in the aviation industry already knew: As the hot-selling 777 takes off, Boeing is soaring ahead of rivals.

But a four-month investigation by BUSINESS WEEK has revealed that, for more than two years, Federal Aviation Administration officials have been engaged in a highly contentious debate about a possible 777 design problem that raises serious safety issues. BUSINESS WEEK reviewed scores of internal FAA documents and held lengthy interviews with numerous midlevel engineers and safety inspectors at the agency, including several who worked directly on the 777 certification project. These sources—most of whom spoke anonymously for this article out of fear of reprisal—say that many FAA officials continue to question whether the plane has been adequately tested. "It's an issue of safety," says one FAA engine specialist, referring to concerns that the 777 could be severely destabilized if a fan blade broke. "It could lead to catastrophe."

DUAL MANDATE. Boeing executives declined to comment for this article. In a written statement, the company maintains that "no airplane in history has been tested as thoroughly as the Boeing 777." Top FAA officials in Washington also vehemently defend the plane. Thomas McSweeney, director of the FAA's aircraft-certification service, says that if he believed the plane was unsafe, he'd have stopped certification "in a heartbeat. The airplane has met every regulation that it was required to meet."

But well-placed FAA sources see the issue differently. They believe that pressure to meet Boeing's planned certification date for the plane—Apr. 19, 1995—led top-level officials at the FAA to overrule safety concerns raised by the agency's own engineers. Keenly aware that Boeing's commercialization schedule depended on meeting that deadline, these sources argue that FAA management granted the 777 an operating certificate without adequately testing for the potential design flaw. Critics say that such problems stem from the agency's dual mandate: The FAA's charter calls for it to ensure the safety of the public as well as to promote the U. S. aviation industry. "The FAA is supposed to regulate the manufacturers to ensure airline safety," complains one FAA inspector. "Washington knows how important that plane is to Boeing's entire existence."

McSweeney denies that contention. While aircraft manufacturers "try to hold to their certification dates," he

WAS THE 777 ADEQUATELY TESTED?

In these excerpts from various FAA documents, agency officials question Boeing's safety data on the 777—and Boeing initially refuses to perform more tests

ISSUE PAPER

PROJECT: Boeing Commercial Airplane Group Model 777 TC0001SE-T
ITEM: A-11
STAGE: 4
REG.REF.: §§ 21.21(b)(2), 25.901(c), & 25.903(c)
DATE: April 18, 1995
NATIONAL POLICY REF.: None
ISSUE STATUS: Closed
SUBJECT: Engine Unbalance Due to Fan Blade Loss
BRANCH ACTION: ANM-120S, 130S, 140S, 160S, AEG
COMPLIANCE TARGET: Pre-TC

The FAA's complaint: Boeing's analysis of a blade break was "inconclusive." The analysis and flight test experience "do not adequately prove that the equipment as installed in the 777 will survive."

Boeing's response: "The analysis and data provided more than substantiate compliance.... Boeing has no intention of doing any further testing."

naintains that the FAA did not rush to neet Boeing's schedule. But this is not he first time the FAA has faced criticism of being too close to planemakers. In a General Accounting Office report on the FAA's certification practices published ast year, the agency was criticized for exercising weak oversight. Normally, he agency works closely with the manufacturer during the final stages of design of a new plane. After conducting light tests and reviewing compliance with FAA regulations, the agency is supposed to approve new planes only when all problems have been worked out.

COZY TIE-UP. But the GAO report criticized the agency for depending extensively on manufacturers' own engineers to approve much certification testing. And Steven Calvo, the report's author, says the GAO also found that the FAA approved new planes even when kinks remained. "At the end, there are lots of things the FAA is trying to resolve, but manufacturers have sold those planes," says Calvo. "They have to make deliveries by specific dates or they face penalties. It's an economic issue."

In the case of the 777, the FAA and Boeing worked together more closely than usual: As part of its strategy for getting the 777 up and flying in record time, Boeing and the FAA agreed to a cooperative certification process from the start. Boeing kept the agency informed of the plane's design at every step, allowing problems to be worked out as they arose.

The debate over safety stems from concerns about the size and weight of the fan blades in the 777's unusually large jet engines. Because the 777 was designed with two engines, rather than the four common in previous long-haul models such as the 747, its fan blades are bigger and far heavier. In their largest configuration, for example, the 777 fan blades built by Pratt & Whitney each weigh 43 pounds—more than three times the weight of those built for the 747.

Therein lies the problem: Numerous FAA engineers and inspectors fear that if one of those giant blades were to break in flight, tremendous vibrations could occur that might severely destabilize the plane. Such breaks are not unknown: 24 other jet airliners have reported fan-blade breaks since 1990. Although no crashes have resulted, FAA safety experts fear that the greater size and weight of the 777's blades would make such a break far more destabilizing. They warn that the 777 cockpit might shake so badly that pilots could not read the flight instruments, increasing the risk of a crash. And the effect on passengers, they say, remains unclear. Indeed, continued concerns have led the FAA to consider new regulations in consultation with the aviation industry.

Despite the worries, FAA sources say Boeing appears to have done only limited testing to see how the 777 would react if a blade broke. And with no regulations on its books specifically requiring such data, the FAA appears to have backed down—days before certification—from a yearlong bid to get Boeing to do more thorough tests. "Boeing did not go beyond the bare minimum requirements," says one FAA engineer.

BIGGEST EVER. Top FAA officials vehemently deny that view. They insist their testing of the 777 was sufficient. McSweeney says the plane would bear no increased risk of destabilizing vibrations if a blade were to break. While the design of the 777 "makes the engine-imbalance issue a little more important to deal with," he maintains it does not increase the chances of pilots' losing control. Instead, he argues that vibrations would be no worse than those on a 747. And he adds that pilots would be able to maintain control simply by lowering the altitude—although FAA sources say that solution is under dispute. The three makers of engines for the 777—Pratt & Whitney, General Electric, and Rolls-Royce—also deny any problems. "We're confident this is a completely reliable and dependable aircraft-engine combination," says a Pratt & Whitney spokesman.

For now, Boeing is the only manufacturer to face such questions because the 777 engine is the largest engine ever put on a commercial aircraft. But the industry trend is moving toward bigger engines, and rivals won't escape the debate. "This is not just a Boeing problem," says Thomas Boudreau, an FAA engineer who worked closely on 777 certification.

The new 777 series is central to Boeing's effort to maintain its lead in the global market. With 350 to 400 seats, the 777 competes with the A-340 and A-330 jumbos produced by the Euro-

pean consortium Airbus Industrie and with the MD-11 from St. Louis' McDonnell Douglas Corp. With world demand estimated at more than 3,000 for such jumbos over the next two decades, Boeing counts on the 777 to fuel growth for years. It "will be Boeing's most important product," says Edmund S. Greenslet, publisher of *Airline Monitor* in Ponte-Vedra Beach, Fla. By 2000, he estimates the 777 will account for $12 billion in annual sales—40% of Boeing's projected new-aircraft revenues.

The 777 promises a bonanza for the airlines, too. Analyst William B. Whitlow Jr. of Portland (Ore.) brokerage Pacific Crest Securities estimates the two-engine plane could cut fuel costs 20% below the 747, even as it carries more cargo and passengers. That has won plenty of customers. United Airlines Inc. ordered 34 and took delivery of the first of them in May. Boeing has sold 245 of the planes to British Airways, Japan Airlines, Continental Airlines, and others. Although aware of the questions about engine imbalance, "we're pleased with the performance of the airplane and of the engine," says Gordon A. McKinzie, United's 777 program manager.

The FAA debate crystallized in November, 1993, when a 747 of Cathay Pacific Airways Ltd. blew a fan blade over the Pacific Ocean. The break produced such severe vibrations that the pilots considered ditching the plane in the sea. Although the aircraft eventually landed safely, the incident alarmed FAA engineers then reviewing the 777. In May, 1994, Darrell M. Pederson, manager of the FAA's transport-airplane directorate, ordered Boeing to prove that a similar fan-blade loss would not "jeopardize the continued safe flight and landing of the 777." Pederson was not permitted by the FAA to comment, but McSweeney now downplays such fears. The Cathay Pacific incident was made out to be "far more serious" than it was, he says.

EXCUSES, EXCUSES. Nevertheless, over the following year the FAA sent a stream of letters to Boeing asking for such proof. FAA officials complained about Boeing's lack of response: Donald E. Gonder, manager of the airframe branch of the FAA's aircraft-certification office in Seattle, wrote in one internal document that Boeing always had "one excuse or another" for not providing the data. Finally, in a letter dated Jan. 25, 1995, Donald L. Riggin, manager of the FAA's Seattle office, warned Boeing that if it wanted to win 777 certification on Apr. 19, it was "imperative" to provide answers by Jan. 31. Neither Gonder nor Riggin would comment.

Boeing's response came on Feb. 7. In a letter to Riggin, Timothy E. Hickcox, Boeing's 777 certification manager, acknowledged that Boeing was also concerned about the effects of an unbalanced engine. But he argued that Boeing had looked into the issue and considered the plane safe, although it was "without documentation" to demonstrate its claim—since it was under no "regulatory requirement" to provide it.

777 SALES TAKE OFF

	FIRM ORDERS	OPTIONS
UNITED AIRLINES	34	34
SINGAPORE AIRLINES	28	33
ALL NIPPON AIRWAYS	28	12
SAUDIA	23	
BRITISH AIRWAYS	15	15
JAPAN AIRLINES	15	10
MALAYSIA AIRLINES	15	
THAI AIRWAYS	14	
CATHAY PACIFIC AIRWAYS	11	11
KOREAN AIR	12	8
OTHERS	50	27
TOTAL	245	150

DATA: FEDEX AVIATION SERVICES INC

BOEING'S FUTURE HINGES ON THE 777

Under continued pressure from FAA engineers, however, Boeing partially relented. On Feb. 16, Boeing gave the agency information that it claimed showed the level of vibrations a 777 would suffer if a fan blade did break. In a letter, Hickcox argued that the expected vibrations would be "reasonable"—so minor that passengers and pilots would remain safe.

But the letter did little to mollify FAA engineers. In numerous documents, the FAA argued that Boeing had simply asserted its findings without providing data to back them up. In one briefing paper, FAA engineer Jeffrey E. Duven complained that Boeing's findings were "incomplete" and unlikely to provide "credible validation" of its claims. And in a Mar. 4, 1995, letter, the FAA warned that Boeing's analysis was "inconclusive" and that it "[does] not adequately prove that the equipment as installed in the 777 will survive" the vibration levels Boeing projected.

A month later, FAA engineers were still waiting. According to an internal memo dated Apr. 10—just nine days before certification—the FAA warned Boeing that the plane could not be approved without such data. But Boeing again dismissed the demands. "The analysis and data provided more than substantiate compliance," Boeing responded. "Therefore, there is no need for additional testing, and Boeing has no intention of doing any further testing."

"HARSH RHETORIC." McSweeney describes such discussions as common. "It's the give-and-take in the certification process that leads to the safety we have today," he says. But other FAA officials argue that such a late, heated exchange is unusual. "There's always a certain amount of disagreement," says Jack A. Sain, who retired in 1993 as the manager of the FAA's North East propeller and engine directorate, the primary unit responsible for engine certifications. "But generally, a certification doesn't degenerate into such harsh rhetoric."

In a meeting on Apr. 12, FAA engineers specified several tests Boeing still needed to do to allay its concerns: The FAA asked for a "full airplane test" in the air to show that the plane could continue to function. The FAA also asked Boeing to do a flight-deck simulation using the expected level of vibrations over an extended time period, to show that pilots would be able to read their instruments. And they asked about potential for injuries to passengers.

Finally, on Apr. 13 and 14, Boeing submitted additional documentation. In response to demands for a full plane test, McSweeney says that no live flight test was then done. Instead, Boeing submitted data culled from 1,000 previous flight tests; altogether, Boeing argued, pilots had flown an hour under heavy vibrations with no difficulties. However, the accumulated hour was made up of roughly 100 separate incidents, each lasting no more than 30 seconds.

As for a flight-deck-simulator test showing that pilots and other crew members would be able to perform, Boeing cited engineering studies that it claimed showed that the vibrations would be similar to those experienced on a 747. Boeing also submitted a report from one of its own representa-

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tives. The Boeing rep traveled to several flight simulation facilities and underwent vibration tests at levels that Boeing claimed "were representative of blade-out windmilling vibrations." After its own rep reported that he had no trouble reading, writing, or speaking during the vibrations, Boeing argued that there was no need for further testing. As for passengers, Boeing again concluded that, under the worst vibration levels it estimated, such levels "would not cause injury to passengers."

Apparently, that was enough to satisfy top FAA officials. On Apr. 18, Pederson agreed that Boeing had provided adequate data. The next day, the plane won certification on schedule.

NEW RULES? But critics within the agency say the tests Boeing submitted remained far below the standard they had demanded for more than a year—and did little to allay their fears. One FAA inspector closely involved in the 777 certification dismisses the 747 comparison as "apples to oranges." He and others also say that such tests do not recreate the vibration levels pilots would experience over a lengthy time period. "Unless you put a dummy in a seat and shake it for an extended period of time at expected levels, you haven't proved a thing," says the inspector.

McSweeney defends the decision to move ahead with the certification. "[Engine imbalance] is a fairly new issue," he says. "We're all learning all the time." Indeed, the subject has become one of the main agenda items of the Aviation Rulemaking Advisory Committee (ARAC), a quasi-official advisory group of aviation-industry and FAA officials that develops new airline regulations. The group is studying possible changes in FAA rules needed to deal with the dangers of imbalance typified by larger engines. Numerous ARAC group members acknowledge that current regulations—developed in the 1950s, when fan blades were far smaller—do not require adequate testing for large engines. "Imbalance is more of an issue than it was in the past," says Larry Hanson, manager of loads and dynamics for Gulfstream Aerospace Corp. in Savannah, Ga. "We're still reviewing what the requirements ought to be."

The FAA's McSweeney agrees there is a need for more study. "We started this debate; we wanted this debate," he says. One remedy being considered, alongside a drop in the plane's altitude: requiring explosive bolts to be installed, so that in an emergency the affected engine would be blown off the wing. Until these safety issues are more clearly resolved, that may be the best the FAA has to offer.

By Christina Del Valle and Michael Schroeder in Washington

INITIAL PUBLIC OFFERINGS

MORE INTERNET IPOs, ANYBODY?

A second wave is coming, but investors are more chary

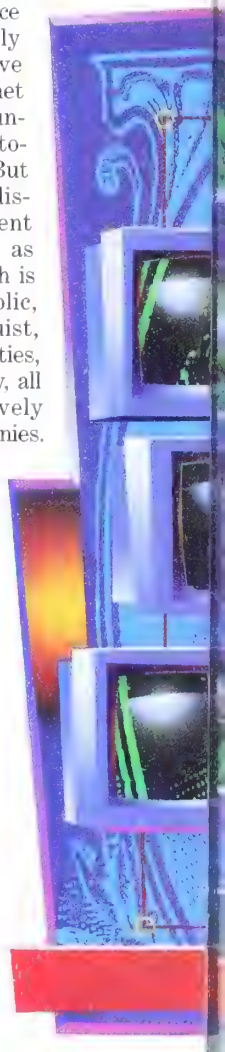
Behind Howard S. Jonas' scuffed metal desk is a poster for the movie *Field of Dreams*—about a man who builds a ball field in the middle of nowhere in the belief that "if you build it, they will come." Jonas is chief executive of IDT Corp., an Internet company in Hackensack, N.J. Instead of a ballpark, Jonas is pinning his hopes on the vastnesses of the Internet—and an inch-thick document on his desk. It is an initial public offering prospectus.

Jonas is betting investors will flock to his stock offering—and he's not alone. Yep, they're back. Internet IPOs, the fuel that stoked the fired-up stock market of 1995, are about to make another charge through Wall Street, despite the recent poor performance of Net stocks. The *Interactive Week*-American Stock Exchange Internet index, which gained some 130% in 1995, has declined 10% since its peak in early December as investors began to focus on superhigh valuations—and mounting competition—among such hot Net stocks as Netscape Communications, Netcom Online Communication Services, and PSINet.

But even as share prices soften, the dealmaking continues to be intense—and the effect will be seen on the Street in coming weeks and months. The new crop of stock issuers include Jonas' IDT, an Internet services provider and discount telephone company; CyberCash Inc., which provides security for online transactions; Raptor Systems, a maker of antihacker software; and VocalTec Ltd., an Israeli company that is pioneering in the potentially explosive field of voice communications over the Net.

All have registered IPOs with the Securities & Exchange Commission in recent weeks, and others are expected to join them soon. The fate of these IPOs, however, is far from certain. They stand a good chance of being rejected by an increasingly chary market that is unlikely to produce another Netscape—which went public at 28 in August and hit 171 in early December before falling to 140 or so. Even worse declines were suffered by Netcom, UUnet, and other Internet service providers—companies that hook people up to the Net.

HUMMING. The service providers are easily the most competitive sector of the Internet business, with hundreds going head-to-head nationwide. But that has hardly discouraged investment bankers such as Cowen & Co., which is bringing IDT public, Hambrecht & Quist, Montgomery Securities, and Morgan Stanley, all of which are actively courting Net companies. Yahoo! Corp., which publishes an online guide to Web sites, is one



The action—and competition—is hottest among Internet service providers, which are in need of big bucks for expansion

' the companies that is be-
eved to be heading toward a
ock offering, and so is Lycos
ıc., a Web-page search service
ıd subsidiary of CMG Informa-
on Services. "Everybody
ants to give you money," says
ill Pendley, chief financial offi-
er of Digital Express Group, a
ivately held internet provider
Beltsville, Md.

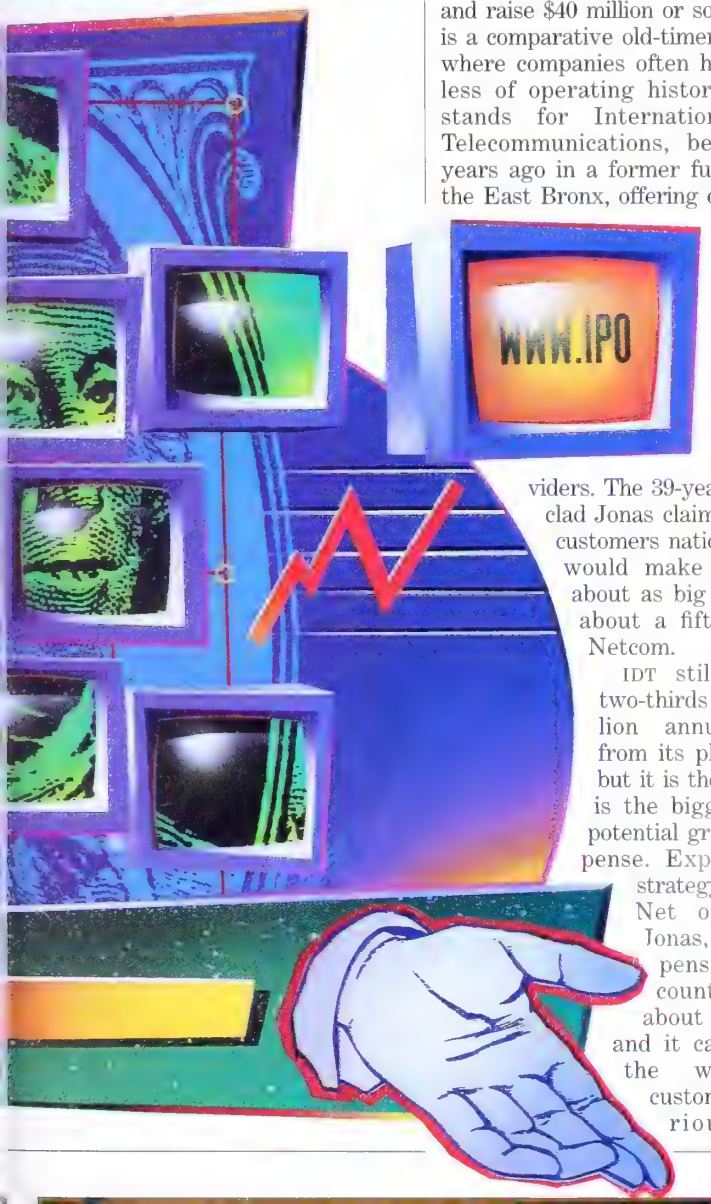
Why are Internet IPOs pick-
g up despite the malaise
nong Net stocks? Some of it
, of course, old-fashioned transaction
ınger among investment bankers. The
ıternet IPOs were among the most suc-
essful stock offerings in recent history,
terms of both commissions and af-
ırmarket performance. And there is a
ırresponding hunger for capital among
et service providers, which are grow-
g at an astounding rate. According to
organ Stanley & Co., the number of
ıstomers of the Internet-only services
ıs grown nearly sixfold—from 92,000 to 523,000—in just the past year or so. Most Net providers have raised capital mainly through bank borrowing and venture capital. Digital Express, for example, has gotten funding from Venrock Enterprises—the Rockefeller family's venture-capital outfit—while IDT drew the interest, and cash, of money manager Mario Gabelli.

ANOTHER NETSCAPE? PROBABLY NOT, BUT...

COMPANY	UNDERWRITER	DESCRIPTION
C/NET INC.	N. A.	Easiest way to get shareware over the Net
CYBERCASH	Hambrecht & Quist	Pioneer in making the Net a global shopping mall
IDT CORP.	Cowen & Co.	Telephone upstart turned Internet provider
RAPTOR SYSTEMS	Montgomery Securities	Designs software to make the Net more secure
VOCALTEC LTD.	Hambrecht & Quist	Pioneering voice communication over the Net
YAHOO! CORP.	N. A.	The Internet's best-known indexing service

DATA: BUSINESS WEEK

A good example of the evolution of these companies is provided by IDT, which plans to sell 4.6 million shares and raise $40 million or so in its IPO. IDT is a comparative old-timer in a business where companies often have a year or less of operating history. IDT, which stands for International Discount Telecommunications, began life five years ago in a former funeral home in the East Bronx, offering discount trans-Atlantic telephone service. Jonas moved to Hackensack in 1992 and was one of the first Internet-only service providers. The 39-year-old, sneaker-clad Jonas claims some 50,000 customers nationwide—which would make his company about as big as PSINet and about a fifth the size of Netcom.



IDT still gets about two-thirds of its $40 million annual revenues from its phone business, but it is the Internet that is the biggest source of potential growth—and expense. Expansion is the strategy of aggressive Net operators like Jonas, and it is expensive. Each account brings in about $30 a month, and it can vanish like the wind—Internet customers are notoriously fickle. Jonas notes that it costs him some $150 to take on a new account—half in marketing expenses, half in new equipment. For example, a high-grade modem, costing upwards of $400, must be bought for every 15 new clients. So if IDT were to expand by, say, 20,000 new clients, it would require some $3 million—and that would have to come from somewhere. "In a way, Wall Street determines who will be the big players," Jonas says.

SEARCH AND DEPLOY. One Internet company itching to become a big player is San Francisco-based c/net Inc. That's c as in "content"—which is what distinguishes it from other Internet ventures that have gone public. The three-year-old company's game plan is to provide a Web page that people eventually will pay for—either as subscribers or advertisers. c/net is headed by two former college roommates, CEO Halsey Minor and CFO Shelby Bonnie, who was managing director of the Lynx Partners venture capital fund at Tiger Management Corp., headed by famed investor Julian H. Robertson Jr. c/net hosts a show about the Internet on the USA cable network, and its seven-month-old Web site provides, among other things, an easy method of searching for and downloading thousands of shareware files—free or low-cost software—scattered around the world but accessible via the Internet. A c/net official says talks have been held with Morgan Stanley, though Bonnie says there are "no current plans to go public."

If c/net stays private, and some other IPO plans fall through, it will be good for the survivors. "If you get too many of these Internet IPOs, you could saturate the industry," observes Arthur Bonnel, portfolio manager of the Bonnel Growth Fund. That would add to the downward pressure on Internet stocks.

Jonas has another poster behind his desk: *Man of La Mancha*. Is Jonas tilting at windmills—or will investors flock to IDT as they did to Netscape and Netcom? Investors have short memories—and for the ones who bought Internet stocks at their dizzying highs, they are crummy memories indeed.

By Gary Weiss in New York

INVESTMENT FUNDS

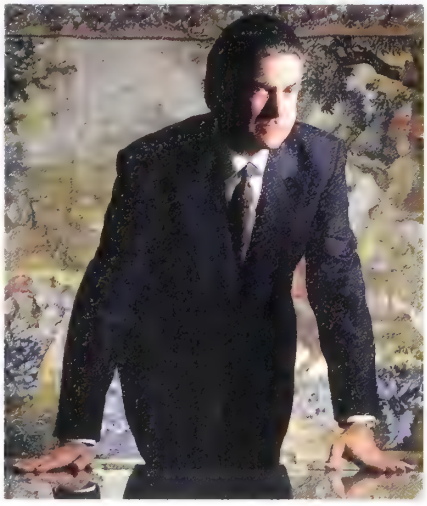
A HIGH-WIRE ACT IN HIGH TECH

Amerindo's bet in cutting-edge companies is paying off big

When a blizzard of selling in technology stocks led the market sharply downward in early January, Alberto W. Vilar, president of San Francisco-based Amerindo Investment Advisors Inc., barely flinched.

"It's no fun to see your stocks get clobbered," says Vilar, whose firm, with about $2.5 billion in assets under management, is one of a few major U.S. money-management concerns that invests exclusively in specialized emerging-technology issues. But Vilar, 55, had seen it all before. As Fidelity Investments and other institutional investors were paring their high-tech holdings, Amerindo went shopping—as it has done frequently since its founding in 1980. "Corrections are a way of life," Vilar says. "We were out there with our basket when these things were being tossed out."

EARLY TRACKING. This aggressive strategy is not for the faint of heart. But for Amerindo, it has paid off handsomely: With a return of 91.2% for 1995, based on holdings at the end of the third quarter, Amerindo ranked first among 818 U.S. money managers, according to Thomson Investment Software, a portfolio-performance information service.



RELIGIOUS ZEAL: *Vilar loves the Net*

It also ranked seventh out of 563 managers for the last three years with an annualized return of 42%. "These guys have been outstanding in their research," says Marty B. Tolep, a senior vice-president of Smith Affiliated Capital Corp., a fixed-income management firm, and former pension-fund manager at Woolworth Corp., an Amerindo client.

Amerindo's faith in technology generally and the long-term potential of the Internet in particular is almost religious. Most of Amerindo's portfolio is invested in biotech, telecommunications, and software issues, many of them makers of networking and Internet software. He is the biggest public shareholder of Netscape Communications Corp. and holds large stakes in Cisco Systems, Ascend Communications, Fore Systems, PsiNet, Premisys Communications, and America Online.

Amerindo starts tracking hot technology companies years before they go public. The firm's seven analysts, most of whom have advanced degrees in engineering and science, focus on companies financed by top venture-capital firms such as Institutional Venture Partners, Mayfield Fund, and Sequoia Capital. He also tends to buy initial public offerings underwritten by a select fraternity of investment banks, notably Morgan Stanley, Hambrecht & Quist, and Robertson Stephens. In years of buying newly public companies, he has found that if Wall Street's earnings estimates before a company goes public exceed its performance in its first few public quarters, chances are its share price won't rise any further.

Vilar isn't worried about technology issues plateauing soon. One indicator he watches is the price-earnings ratio of the benchmark T. Rowe Price New Era Fund compared with the p-e of the S&P 500 index. When it hits 2.0, technology stocks tend to be fully valued, Vilar says. At the current 1.5 level, he says, there's still a lot more money to be made.

By Phillip L. Zweig in New York

MUTUAL FUNDS

IS MIKE PRICE CASHING OUT?

The buzz: He wants to go from funds to direct investments

Superstar Michael F. Price may be looking to exit the mutual-fund business. Investment banking sources say Price has hired Goldman, Sachs & Co. to find a buyer for his firm, Heine Securities Corp., parent of the $13 billion Mutual Series Funds. Price declined to comment, as did Goldman.

But several bankers who work with financial companies say Heine Securities is on the block. The word is that Price, 44, wants his money out so he can personally make investments that rattle stodgy companies. His most recent success: Chase Manhattan Corp. Last spring, Price's funds acquired a 6.1% stake in Chase and prodded the company into a merger with Chemical Banking Corp. So far, his funds have earned more than $300 million on Chase alone. Such investing has logged superior results. For the 5- and 10-year periods ending Dec. 31, Price's returns are in the top 10% of all funds.

Heine's revenues come mainly from fund advisory fees, which could run as high as $80 million this year. A. Michael Lipper of Lipper Analytical Services Inc. says that based on revenues, Price's price could be well in excess of $100 million—perhaps more than $200 million if the payment is stretched out over a number of years, tied to performance incentives and revenue growth. Several investment bankers think Heine could fetch 50% to 100% more.

PRICE: *Logging in top returns*

Price may have a hard time getting out the door. His eclectic investment style, which includes investing in bankruptcies and mergers, is hard to duplicate. Price has a strong research team in his Short Hills (N.J.) headquarters, but it isn't certain if the results would be the same without him. Worse yet, shareholders might bolt if Price leaves. Says one banker: "I'm not sure you could get top dollar for the funds unless Mike Price signed a very long contract to manage the funds."

By Jeffrey M. Laderman with Kelley Holland, in New York

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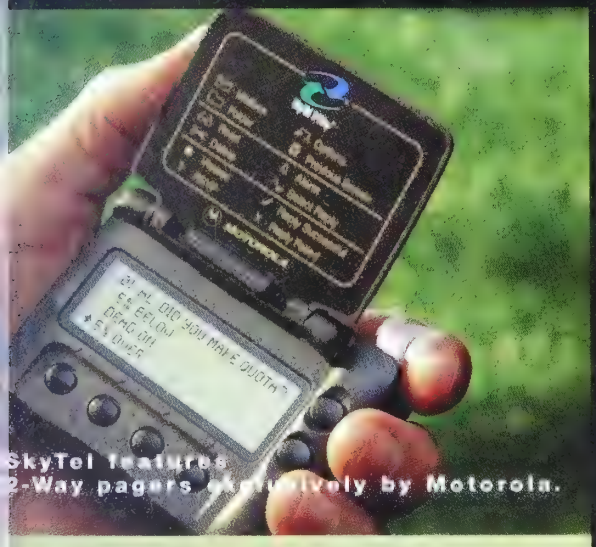

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INTEREST RATES

THIS SURE THING ISN'T SO SURE ANYMORE

A yield play may come undone

Could Wall Street's hedge funds spoil the party in the U.S. bond market? A growing number of experts fear it's possible. The trigger: a wildly popular arbitrage trading strategy involving Japanese and U.S. securities.

The risky play was inspired last September, when the Bank of Japan halved short-term interest rates to just 0.5% to boost the country's economy and its crippled banks. Officials hoped bankers would invest their low-interest loans in U.S. Treasuries yielding 5% to 6%. The implicit understanding: The central bank would minimize currency swings that could lower the return.

Japan's banks remained skeptical. While they profited from the wider yield spread at home between short-term bills and long-term bonds, they largely have shunned U.S. Treasuries. But hedge fund managers just loved the play. Such leading moneymen as George Soros, Julian Robertson, Paul Tudor Jones, and John M. Meriwether are thought to have plowed their yen borrowings into U.S. Treasuries, primarily 2- to 10-year bonds then yielding from 5.6% to 5.95%.

SEVEN-YEAR HITCH. The strategy is working beautifully so far. The U.S. bond market has rallied, increasing the value of the hedge funds' holdings. Also, the dollar is flirting with 106 yen, up from 101 in September. And the yield spread is still around four percentage points. By leveraging as much as 100% of the trade and not hedging against currency risk, the funds are believed to be reaping 30% to 60% annualized returns. "This trade is a good deal as long as you believe Japan is not going to tighten [credit] anytime soon," says one fund manager.

But their gamble could backfire. For one thing, a critical assumption behind the strategy—that Congress and the White House will agree to balance the budget in seven years—now looks dicey. Some currency traders worry that if the budget talks collapse, the dollar might fall as much as 10% against the yen. At that point, the highly leveraged funds would have to repay the yen they borrowed to buy Treasuries with. The result could be a rush for the exits as traders dump Treasuries to meet their margin requirements. "If the budget negotiations collapse, get out of the way," warns Daniel J. Fuss, head of fixed income at Boston-based Loomis, Sayles & Co. Some funds are already rumored to be frantically trying to unwind their Treasury holdings.

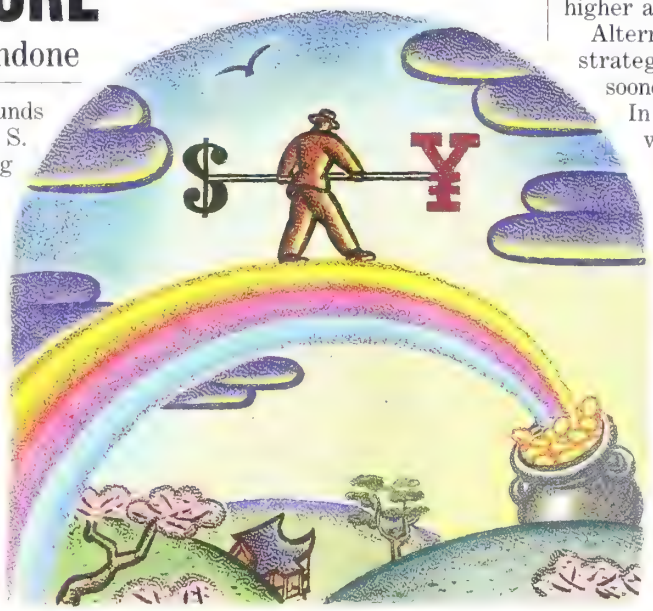
The U.S. budget is not the only great unknown. Japan's banking crisis is now the problem of newly appointed Prime Minister Ryutaro Hashimoto. If a proposed bailout plan for the troubled housing-loan companies unravels, says Soros, "you would be back to a crisis situation in Japan." The long-awaited economic recovery could be choked off for lack of credit. That would stifle imports, drive Japan's trade surplus back up, and push the yen higher again.

Alternatively, Japan's cheap-money strategy could revive the economy sooner than the hedge funds expect. In that case, the Bank of Japan would have to raise rates to prevent a surge in speculative activity. It wouldn't be the first time fund managers got burned by a monetary about-face. In 1992-93, when the Federal Reserve kept rates on overnight loans at 3%, hedge funds made billions borrowing short-term and investing in long-term bonds. But in early 1994, the Fed began raising short-term rates, tightening all year until they hit 6%. Many hedge funds, caught off guard by the Fed move, absorbed huge losses and had to dump Treasuries to make themselves whole. The result: a bond-market tailspin unseen since the 1920s, as funds sold off Treasuries in droves.

How much is riding on the dollar-yen bet? Exact figures are hard to come by because many hedge funds bought swap and repurchase agreements, which don't show up in government capital-flow reports, rather than the underlying securities. But market pros estimate that the combined exposure could top $70 billion. Ronald Bevacqua, economist at Merrill Lynch & Co. in Tokyo, says that yen-denominated borrowing from abroad jumped by more than 30% from the third quarter of 1994 to the third quarter of 1995, when Japanese short-term rates fell.

For now, the yen-dollar arbitrage looks like a sure thing. But that's often a sign that the easy money has been made. If either the U.S. government or Bank of Japan changes course abruptly, the gamblers may have to fold their cards.

By Dean Foust in Washington, with Brian Bremner in Tokyo



DELICATE BALANCE "If the budget negotiations collapse, get out of the way," says one fund manager

THE BET

- Investors borrow in the Japanese money market, at interest rates less than 0.5%. They then buy U.S. Treasuries, yielding near 6%.
- They heighten their gains by leveraging their accounts—buying Treasuries on margin.
- They don't hedge against currency risk.
- As long as rates and currencies remain stable, the spread gives investors up to 60% returns.

DATA: BUSINESS WEEK

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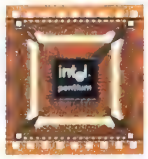

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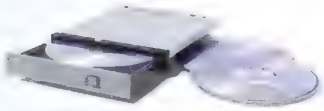

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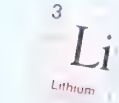

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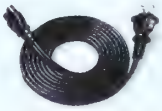

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INVESTING

'WE ONLY TAKE MONEY WITH BRAINS ATTACHED TO IT'

Broker Steven Abernathy gets ideas from MDs, not MBAs

When Steven H. Abernathy talks about interactive investing, those who knew him in his former career might flinch. But the boxer-turned-broker's idea of a useful contact has changed dramatically since the early 1980s.

Rather than relishing a good right jab, the contact he now values is bouncing ideas off the healthcare and technology professionals that invest in the Steven Abernathy Group, a private client group at Manhattan-based investment firm Cowen & Co. He credits his stable of doctors and technology execs with providing an information edge that helped his aggressive accounts rack up a 45%-plus return in 1995 and an annual compound return of about 65% over the past five years.

ABERNATHY & LEET: *Their five-year return is more than double that of diversified health and tech mutual funds*

SOUNDING BOARDS. But while most money managers consider themselves the pros and care little about the expertise of their clients, Abernathy and his colleague, Gary Leet, take a different approach. They say they will not manage someone's money unless that person can be helpful in, say, evaluating medical devices or new software being developed by companies that are not heavily followed by the Street. "We only take money with brains attached to it," says Leet. Clients act as sounding boards, he says, providing information on trends and products that may lead to investments. The group manages $90 million for 110 accounts.

With annual total returns ranging from 147.2% in 1993 to -6.3% in 1994, and holdings of just 8 to 12 stocks, Abernathy's growth style is risky. He doesn't believe diversification is the best way to lower risk. "The most effective way to reduce risk is to increase information," he says. And he feels he has the best information available. Whether it's because of superior information or some other factor, his five-year record even outshines the 28.4% average five-year return for the diversified technology funds tracked by Morningstar Inc.

Abernathy says he is a long-term investor, but he had some good short-term wins last year: managed healthcare company Pacificare Health Systems, which he bought as it rose from 53 to 62 and then sold four months later at prices ranging from 79 to 85; Respironics, a maker of medical devices which he purchased at prices from 9 to 13 and which closed 1995 at 21; and Genetics Institute, bought around 38 and sold two months later at about 50.

Abernathy and Leet say information from their clients sometimes helps them avoid losing money. Abernathy thought a laparoscopic surgery device that U.S. Surgical Corp. made could be a winner. But after speaking to clients such as surgeon John Reeder he discovered that U.S. Surgical's pricing was being undercut. Instead of their competitor cutting the price of a similar device, however, it was discounting items that were bundled with the device and sold to hospitals. That made the competitor's inroads harder to spot. "That information stopped us from making a terribly costly error," says Abernathy.

BONING UP. More recently, an orthopedic surgeon gave Abernathy an idea. The surgeon was talking about osteoporosis and mentioned a new drug that adds density to bones. He added that there are ways to test bone density, but that the testing has not been widely used, since there was no real way to treat the disease. With the new drug coming out, "we thought—what companies are the best at testing bone density?," says Abernathy. "There are some very good, young companies that could make a ton of money." Abernathy will not divulge company names because he has not yet decided where to invest.

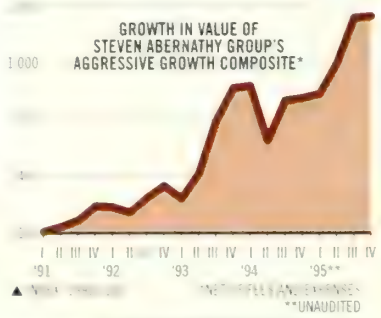
His clients didn't help him avoid a dismal return in 1994. That year, he shorted semiconductor stocks. But instead of stock prices falling, prices rose and played a big role in the year's 6.3% loss.

Now, Abernathy is again looking at semiconductors—betting that stock prices will rise. But here he is relying on the research of his firm, Cowen & Co., not on clients. "Applied Materials Inc. is being wrongly slammed," he says, having fallen almost 40% in six months. He thinks semiconductor demand will be stronger than expected. Another pick: Abbott Laboratories, which Abernathy says is a good value at 38¾. He still likes Respironics—despite its big gain.

Abernathy has an impressive record, but the bull market must get a lot of the credit. And with tech stocks starting 1996 on a sour note, Abernathy will have to make all the right moves in order to avoid the market's blows.

By Suzanne Woolley in New York

AN Rx FOR RETURNS



DATA: STEVEN ABERNATHY GROUP

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GREEN MONSTER."

'We wanted the whole experience to be like the park itself. It's been called a shrine to the game of baseball. And it is absolutely New England," John Buckley of the Boston Red Sox recalled. John added, "The food had to enhance the experience. That's all we said. That was our direction. And they took off from there. Before we knew it, we were all talking one-on-one with loyal Red Sox fans. A ton of ideas followed. New ways of doing things. We were grilling chicken and selling it all. The chowder was receiving rave reviews. And all of it – every idea they had – fit perfectly at Fenway." At ARAMARK, we believe pre-packaged solutions would be fine if there were such a thing as pre-packaged problems. Instead, we learn our partners' business. And we help them pursue their dreams and goals with an attitude absent of limits. It's moved John to also say, "Last year they helped us increase sales by 17%. Second in the league. But all they can say is, 'Wait 'til next year.

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BY GENE G. MARCIAL

BRIGHT VISTAS AT GREY ADVERTISING

You might think a stock nearing 200 a share was a hot Internet IPO. This one isn't. Grey Advertising (GREY) is a big-time agency, with global billings of $5 billion a year. But that lofty price isn't due to Wall Street fans. The Street is, at best, indifferent: No major firm bothers to follow Grey.

So why are some pros accumulating shares? They say Street indifference is one reason they're high on Grey, which closed at 194 on Jan. 16. This

suggests that not much is known about Grey's growth potential, explains one investor. "In spite of its high price, Grey is still undiscovered and undervalued," asserts Jerome Ballan, portfolio manager at Fahnestock, a New York securities firm. He believes that, based on its "huge earnings-growth potential, Grey is worth 300 a share."

This healthy company "with a lot of excess cash and very little debt sells at a big discount to its true value partly because of the stock's high price—and the thin float available to the public," explains Ballan. Nearly half the 1.2 million shares are controlled by 68-year-old Chairman Edward Meyer.

One money manager expects a 2-for-1 or 3-for-1 stock split soon—to raise the number of shares outstanding and make the issue more widely held. He thinks the agency "will take one of two paths: split the stock or buy back shares using excess cash, to set the stage for taking the company private." Grey already operates somewhat like a private concern: It is out of touch with the Street and reticent with information about itself.

But this pro also thinks that, at Meyer's age, his goal may be a merger or alliance with a larger agency to give Grey a stronger industry presence. Grey declined comment.

A portfolio manager at Tweedy Browne, a New York investment firm that owns nearly 5% of the stock, says Grey is "the cheapest ad agency we know of—and yet it's a cash-generating business that has achieved pretty steady growth over the years."

The stock is a timely bet for 1996, says Ballan, with increased ad spending sure to flow from the Presidential elections and the Olympics. He notes that Grey has been successful in winning clients lately. In mid-1995, it snared the largest single chunk of business in its history: Candymaker Mars consolidated $250 million in billings at Grey.

Grey's stable includes Procter & Gamble, Seagram, General Foods, Britain's SmithKline Beecham and BAT Industries, and Japan's Mitsubishi.

THEY'RE HOLDING THIS BIOTECH BABY

Here's the familiar pattern for hot new offerings: Trading starts, and the stock shoots up. The underwriter issues a "booster-shot" research report. As the stock continues to fly, the venture capitalists (VCs) bail out. By that yardstick, Creative Biomolecules (CBMI) is unusual: It went public at 7 a share in 1993 and climbed to 11, but big VC groups stayed put—and bought more in the post-IPO period. When the stock reversed course and fell to 3 in mid-1994 in the Street's retreat from biotechs, VCs upped their buying. It has since rallied, closing at 8⅝ on Jan. 16.

What's going on? "We assume that Creative must be on to something if an astute VC group is increasing its exposure instead of bailing out," says Marc Strausberg, editor of *The Livermore Report* in Wilton, Conn., which usually focuses on VCs' negative influence on IPOs.

A big VC investor in Creative is Alan Patricof, who has cashed in on such winners as SunGlass Hut and America Online. He holds a 28% stake in Creative, which is trying to develop breakthrough protein therapies for tissue regeneration and restoration. The company's lead compound, OP-1, is a protein capable of stimulating bone growth for repair or replacement of weakened bone and joint tissue.

The importance of OP-1, says Strausberg, is reflected in the $75 million that its partner in the program, Stryker, a maker of surgical and medical gear, has poured in. Analysts expect positive results from the European pilot trial by yearend. They expect Creative to file for FDA approval of OP-1 in 1997.

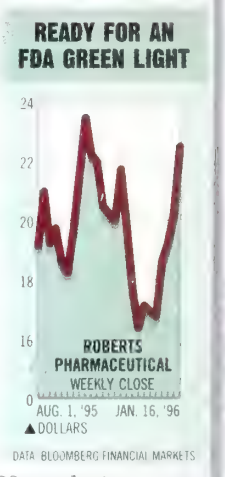
One money manager figures the stock is worth 15 a share.

ROBERTS CAN PLAY HARD-TO-GET

Shares of Roberts Pharmaceutical (RPCX) are showing some life, after languishing in the 16-to-18 range from mid-November to late-December. They closed on Jan. 16 at 22½. One reason: Analysts think the FDA is close to approving Pro-Amatine, Roberts' remedy for low blood pressure. But to some money managers who have snapped up shares in recent weeks, there's a better reason to buy: FDA go-ahead may clear the way for a takeover.

Speculation among some pros is that a European pharmaceutical house with world operations has informally offered 30 a share for Roberts. Whispers are that Roberts top brass nixed the bid, holding out for 35.

One money manager familiar with the situation says Roberts expects the offer will be sweetened to at least 35 once Pro-Amatine gets the FDA's green light. Analysts see Pro-Amatine as a big earnings booster. A spokesman says Roberts is "cautiously optimistic" that it will get FDA approval fairly soon. But he declined to comment on the speculation of a takeover.



From other makers, Roberts acquires drugs that are in their final development phase. It also acquires prescription and OTC drugs already on the market. Its portfolio includes 28 products concentrated in six fields, including oncology, gynecology-endocrinology, and cardiovascular. Roberts' rumored suitor develops, makes, and sells pharmaceutical, diagnostic, and medical-nutritional products. And it has facilities in the U.S., Europe, and Asia.

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LOTUS IS LEARNING TO LIVE WITH THE NET

Defying recent forecasts, Notes may prosper on the Web

Notes is dead. Long live the Internet. No sooner had IBM shelled out $3.5 billion in July for Lotus Development Corp. to get the company's Notes software business than the buzz began: With the Internet's World Wide Web spreading everywhere and taking on new powers, the costly, complex Lotus "groupware" program was history—and IBM would not get the boost in network computing it seeks, or a payback.

By fall, the Notes-is-dead story had legs. Compaq Computer Corp., one of the highest-profile Notes customers, chose an industry conference to let the world know it planned to dump Notes in favor of the Web for a system to share information with suppliers and distributors. "The Internet will probably offer big cost advantages," declared Compaq CEO Eckhard Pfeiffer.

"That didn't help," grumbles Michael D. Zisman, Lotus' new CEO. Nor did the exodus of Lotus management. Within six months of the IBM acquisition, all of Lotus' top execs were gone—including Jim P. Manzi, who quit after clashing with IBM Chairman Louis V. Gerstner Jr. over IBM software strategy.

Now, it has fallen to Zisman, 47, to convince the world that not only is Notes not a victim of the Web but may prosper because of it. A onetime business school professor, Zisman joined Lotus when it bought his E-mail company, Soft*Switch, in 1994. Zisman acknowledges the tough job ahead. "You can compete with a company, but you can't compete with the Web," he says. "It's like shadow boxing."

LOST IN HYPE? Zisman finds himself surrounded by Internet upstarts—including Netscape Communications Corp.—all saying their software will do what Notes does: let organizations publish and share information for groups of workers across a network. And, because they'll do it on the Web, they promise to do it for a fraction of the cost of Notes—until recently about $3,000 per worker. Corporations are surely interested. Forrester Research Inc. estimates that two-thirds of the world's largest companies are building internal networks based on the Web—so-called intranets.

But, lost in all the hype, Zisman insists, are some important facts. Notes "seats" (PCs using Notes) have doubled in the past six months, to 4.5 million, and are expected to hit 20 million in 1998 (chart). And Notes retains important advantages over the Net challengers, including better security and the ability to synchronize multiple copies of databases.

Interest in the Web has actually made Lotus' job easier in some ways, says Ray Ozzie, the creator of Notes, who says he's committed to staying through the next product upgrade. "All the hype over the past six months has done us a tremendous service by espousing the benefits of collaboration," he asserts.

Still, Zisman understands that the Web isn't going away. Instead of resisting it—as Manzi initially did—he's embracing it. On Dec. 13, Lotus rejiggered its pricing to be more like Web software—an inexpensive "browser" that runs on PCs and a costly program for server computers. The Notes desktop software went from $155 to $69—not as deep a cut as some analysts predicted but "in browser country," says Zisman. The basic server program, for up to 100 desktops, went from $275 to $495. A package for 1,000 desktops is $2,295. "This puts Lotus back in the game," says Eric Brown of Forrester.

At the same time, the company is coming out with products that make smooth connections between Notes and the Internet. InterNotes Web Publisher, released last spring, lets users convert Notes documents into Web format. And Version 4 of Notes, released on

ZISMAN: *Instead of resisting the Web, as Manzi did, he is embracing it*

Jan. 10, includes a browser so Notes users can roam the Web. Lotus developers are scrambling to complete a new version of the Notes server software that will use key Web standards and Sun Microsystems Inc.'s Java. That way, Notes can act as a Web server, and work with any Web browser.

More of the Web plan will be revealed at the company's annual Lotusphere conference, starting Jan. 22 in Orlando. Zisman, who is articulate but sometimes bland, will try his hand at cheerleading—to convince 9,000 customers, analysts, and partners that Notes is more relevant than ever. Gerstner will make an appearance, too. "They must make sure they don't lose the hearts and minds of the marketplace," says a former top executive.

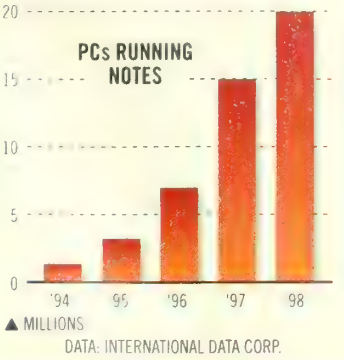
In Orlando, the company will also lay out plans for relaunching its flagging desktop software business. SmartSuite, a bundle of office programs including the Lotus 1-2-3 spreadsheet, is in decline, with just 5% of the market vs. Microsoft Corp.'s 85%. Now, Lotus sees fresh opportunity in "applets"—scaled-down versions of SmartSuite programs that will be delivered electronically over networks—starting midyear. By getting into this new style of software early, Lotus hopes to leapfrog Microsoft.

Does Lotus have a chance? Few Notes customers seem prepared to place all their bets on the Net yet. Many have invested millions in Notes applications and training and say they can't yet duplicate everything Notes does on the Web. So most are sticking with Notes—but experimenting with the Web. "I don't consider it either Notes or the Web," says Jeff Held, a partner in the technology consulting practice of Ernst & Young.

The orders from IBM are to grab as many corporate customers as possible—before the Web grabs them. "Lou Gerstner's directive to me is: Get seats," says Zisman. Lotus and IBM have set a target of 20 million Notes users by the end of 1997, a fivefold increase. "When the number of Notes users breaks 20 million, then IBM's investment will have paid off," says John Jones, an analyst at Salomon Brothers Inc. Then, he figures, Lotus' annual revenue will hit $2.5 billion, generating $500 million in profits. Notes will also help IBM sell network hardware, software, and services to 20 million Notes users. "Clearly, the potential is there for IBM to get its investment back and then some," he says.

To get there, Zisman is devising a sort of Notes Lite strategy. The idea is to start customers out with the Notes E-mail program and then move them up to groupware technology. The first step: persuading companies using Lotus' cc:Mail (about 9 million workers) and IBM OfficeVision (about 7 million) to try Notes for their E-mail. Zisman had pushed hard for this pre-IBM, but Manzi viewed it as a watering-down of Notes. The issue flared into several shouting matches between Zisman and Manzi and other senior execs, according to former Lotus managers.

WEB WORRIES? THE OUTLOOK FOR NOTES IS STILL STRONG



DATA: INTERNATIONAL DATA CORP.

Now that he sits in the corner office, Zisman is pushing the E-mail plan. The new $55 Notes Mail client has the same "look" as Lotus' successful cc:Mail. Customers will need to buy the Notes server software to manage the mail system, giving Lotus a foot in the door.

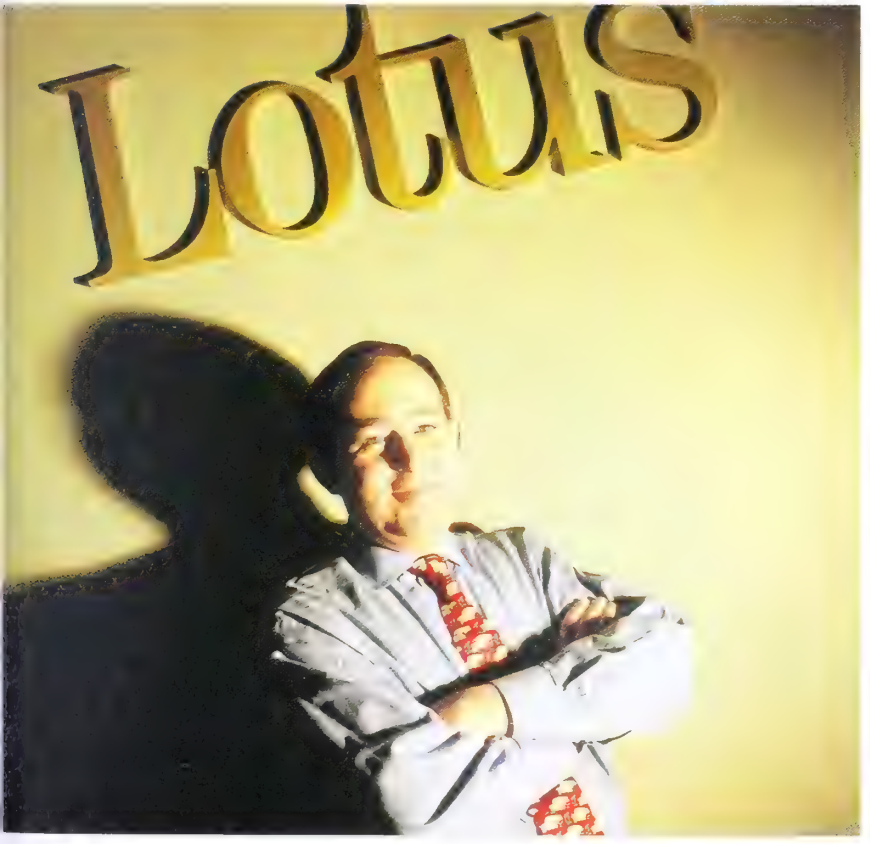
On paper, it looks good. "It's marketing simplicity," says Scott McCready, an analyst with International Data Corp. Before, Notes was a very complicated sell, often part of a consulting firm's "reengineering" plan. That made the price of entry enormous and scared away potential customers.

NEW BATTLE. There is risk to the new approach, however. It pits Lotus more directly against Microsoft. Microsoft Exchange, which was originally intended to be a groupware program, has already been repositioned as a sort of souped-up E-mail setup. Even though Exchange won't ship until later this quarter, Microsoft has been selling the concept hard to customers. Says Zisman: "It will be a slug-it-out war."

At the same time, Microsoft is waging its own battle for the Web. On Jan. 16, it announced plans to buy Vermeer Technologies Inc., a maker of programs for creating Web content. Vermeer will be added to the Microsoft Office suite.

Lotus faces other potential hitches. The parade of departing employees could resume this month when "retention bonus" checks for those who stayed through December are distributed. And many Lotus employees are unhappy that Lotus' generous stock option plan is being swapped for an IBM cash-bonus program based on revenue, profit, and market-share goals. "For people who had options before, and could get them elsewhere, it's a very big deal," says one former Lotus executive. On the other hand, if Lotus makes IBM a success in the networked-computing era, it would be a very big deal indeed.

By Paul C. Judge in Boston



Compaq and IBM haven't decided whether to put value pricing ahead of features or vice versa.

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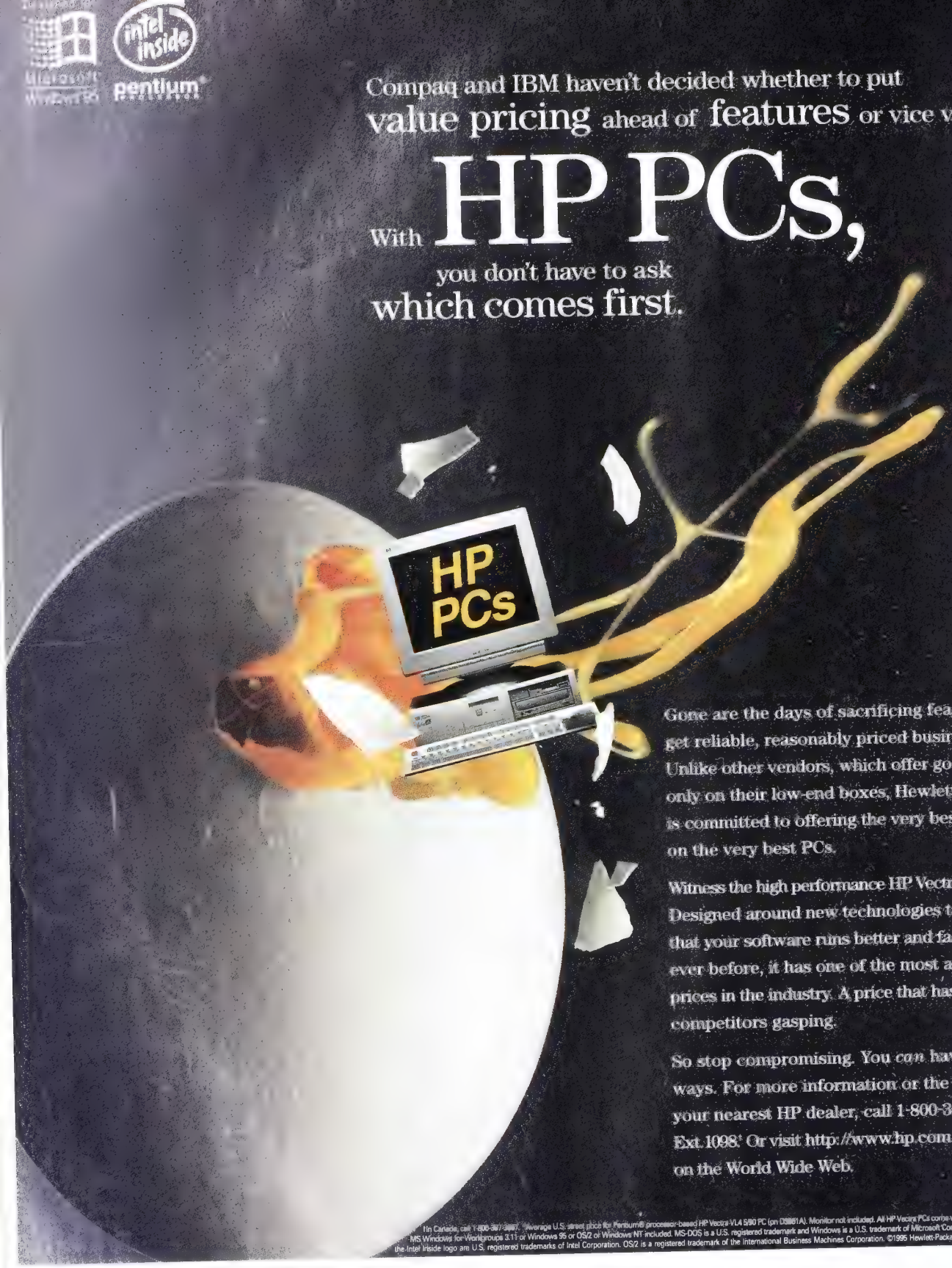

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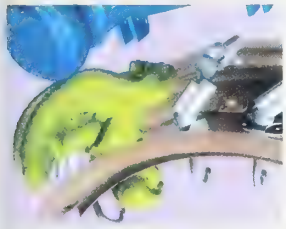
A VIRTUAL REPAIR SHOP FOR ENGINES

IMAGINE DISCOVERING that a new jet engine has to be disassembled just to make everyday repairs—and all because some critical part turns out to be inaccessible. To avoid that awful turn of events, engineers at General Electric Co. used to build mock-ups of engines in the design stage. But a mock-up can cost millions of dollars, and it's difficult for model makers to keep



up-to-date with the latest design revision.

Software can provide the answer. Researchers from General Electric's research and development center and Aircraft Engines unit developed Project Vision, a program that checks designs for ease of repair. Based in part on collaborative work with Stanford University, GE's program shows 3-D images of the volume of air that a part would sweep through as it is wiggled out (yellow area). Anything jutting into that "keep-out zone" would have to be removed first.

Now, GE engineers are working to show the volume swept by tools that are brought in to make repairs. Earlier versions of the software helped design the GE90 engine for Boeing's new 777 jumbo, among other engines.

IS THERE A DYNAMO IN YOUR DRIVEWAY?

BLIZZARDS, HURRICANES, AND OTHER DISASTERS CAN BRING down power lines and plunge your house into darkness. Wouldn't it be nice, mused engineers at Aura Systems Inc., if your home could then draw electrical power from your car?

Turning a car's engine into an auxiliary generator would take only minor revisions, they decided. So technicians at the former defense contractor in El Segundo, Calif., rolled up their sleeves. They tore out the mechanical starter motor and alternator, replacing them with a combined electrical system. Then they added electrical coils to the flywheel, the heavy metal disk that spins to dampen engine vibration, so it could double as an electromagnetic rotor for power generation.

Result: an engine that can easily power an entire household when idling—producing 7,000 watts, says Aura Chief Executive Zvi "Harry" Kurtzman. Aura has applied for a patent and will unveil its engine-generator at the Society of Automotive Engineers show, scheduled for late February in Detroit. The redesign also makes sense for tomorrow's cars, which may need a new source of power if auto makers keep adding more electronic gizmos. Cars already on the road, Kurtzman reckons, could be equipped with power outlets for a few hundred dollars.

INNOVATIONS

■ Each year, 150,000 U.S. women have hysterectomies to stop excessive menstrual bleeding. They may soon have another option: a 10-minute treatment that can be done in a doctor's office under local anesthesia. A balloon is inserted and filled with liquid, which is briefly heated to 190F. The heat removes the lining of the uterus, the main source of bleeding. Developed by Gynecare Inc. in Menlo Park, Calif., the procedure is cheaper and safer than surgery—but it still causes sterility. Clinical trials at 13 hospitals start on Jan. 23.

■ U.S. truckers complain they are being undercut by "sweat-cab" rivals in Mexico, whose drivers flout safety rules when they cross the border and operate in the U.S. To help make sure that Mexican drivers are obeying speed limits and rest-time rules, Diversified Auto Technology in Santa Barbara, Calif., has developed a "black box" recorder. It could be checked at the border and weigh stations if its use were mandated by law—like the black-box recorders in airplanes.

MEMO TO U.S. INVENTORS: FILE EARLY

FOR BASEMENT TINKERERS and corporate researchers alike, the New Year has brought new competition: From now on, overseas inventors will get equal treatment from the U.S. Patent & Trademark Office, ending decades of favoritism. The change was mandated by the General Agreement on Tariffs & Trade and took effect on Jan. 1.

Before that, American patent law stipulated that any research efforts undertaken outside the U.S. could not be used to prove when an invention was conceived. So if an American could document that work on some idea had begun before the date that a foreign researcher applied for a U.S. patent on the same concept, then the American would win—even if the offshore work had started first. (In other countries, there would be no dispute: Patents go to the first party to file, not the first to invent.) For the same reason, overseas inventors never bother to challenge U.S. patents that infringe on their prior work.

The new ground rules mean that research laboratories must be extra diligent in documenting their activities, cautions Jerry D. Voight, a partner at Finnegan, Henderson, Farabow, Garrett & Dunner, a patent-law firm in Washington. The ownership of many patents that earned millions, he notes, was ultimately decided in the courtroom.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwjan@businessweek.com

TELECOMMUNICATIONS

THE BIG DADDY OF DATA HAULERS?

The cable modems on the horizon will easily outspeed ISDN

Stand back when Bill Manuel of Horseheads, N.Y., uses his link to the Information Highway: It's a fire hose. His computer is hooked not to his phone line but to his coaxial television cable, in a technology trial by the local unit of Time Warner Cable. Now, the few times he uses his regular phone modem feel like visits to the Stone Age. Says Manuel, the computing technology director at Corning Community College: "Some downloads take 1½ hours that might take two minutes at most on the cable. It's amazing to start a download with the old modem, go eat dinner, read a newspaper, go back upstairs—and it's still not finished."

Cable modems are still exotica. Only a few thousand people are using them today in trials by cable operators in the U.S., Canada, Japan, and Europe. The nonstandard, first-generation boxes are generally leased, not sold. Aside from that, perhaps 90% of U.S. cable customers are served by networks that can't yet handle two-way data communications. It will be 1997 before a new generation of internationally standardized cable modems will go on sale. And cable operators still must spend billions of dollars to upgrade their networks. The result: Forrester Research Inc. predicts about 6.8 million U.S. homes will have cable modems by 2000.

VIDEO-RICH SERVICES. The mere advent of the cable modem is spurring dramatic improvements in how people tap into the Internet and telecommute (table). The phone companies' ISDN digital-phone-line service is much slower than Manuel's cable link, which handles 4 megabits of data a second. But ISDN, the integrated services digital network, has a headstart and is growing at healthy rates after a decade of being stuck in neutral (box). ADSL, or asymmetric digital subscriber line, can squeeze still more speed than ISDN out of conventional phone wires over short distances. Some well-heeled Net folk are even spending $350 and up monthly for so-called T1 phone lines that handle 1.5 megabits per second. (Manuel pays $25 a month, and an ISDN line might run $50.) Also competing to rain data down on homes are satellite operators such as Hughes Network Systems Inc., whose DirecPC service sends information to two-foot-wide dishes at ISDN-like speeds.

Breaking the data bottleneck will help the entire computer industry. For one thing, it will boost providers of online information and entertainment. The World Wide Web, whose pages are kept fairly simple now to limit download times, will be capable of carrying far more sound, pictures, and video. The video-rich online service planned by Microsoft Corp. and NBC Inc., for instance, would be inconceivable without the prospect of a big jump in data rates to the home. No. 1 cable operator Tele-Communications Inc. is counting on cable modems as on-ramps for @Home, a joint-venture network under development with venture-capital firm Kleiner Perkins Caufield & Byers.

Faster transmission speeds to the home could trigger an avalanche of spending on new computer hardware. That's why Intel Corp. is one of the biggest supporters of cable modems and the like. Once the pathway to the home is widened, other bottlenecks will become more conspicuous, and pressure for upgrades will grow. For example, power surfers will hit Web sites even more often than they do now, forcing the installation of more Internet routers and servers to relieve the inevitable congestion.

Of all the new high-speed technologies, the cable modem has become the most likely to succeed. Cable operators have slowed down their ambitious plans to provide interactive TV, telephone ser-

Reaching Out To Plug In The Home

METHOD	TIME TO DOWNLOAD 10-MEGABYTE VIDEO CLIP	AVAILABILITY	COMMENTS
PHONE MODEMS	14.4 kilobit–93 minutes 28.8 kilobit–46 minutes	Everywhere	Slow but cheap—and the most common option
ISDN	10 minutes	80% of U.S. phone customers	Still complex to install and not especially fast
DIRECPC	10 minutes	Everywhere	The satellite system is only for downloads
T1 TELEPHONE CIRCUIT	52 seconds	Everywhere, at a price	Efficient for companies, costly for homes
CABLE-TV MODEM	20 seconds	10% of U.S. cable customers	Should be used in 6 million homes by 2000

DATA: BUSINESS WEEK, NORTHERN BUSINESS INFORMATION

ce, and videoconferencing. Instead, ey're focusing on the technologically mpler task of providing fat data pelines. These don't require any cost- telephone switches—just routers that ok at the addresses on packets of data id send them off in the right direc- on. Plus, there's none of the regulatory fficulty associated with phone service.

As for the customer's side of the net- ork, a cable modem is fundamentally no ore complex than today's 28.8 kilobit- er-second modems. Although cable odems cost about $400 now in limited iantities, they should come down to out $150, says Mario P. Vecchi, senior ce-president and chief technology officer Excalibur Group, a Time Warner- wned company that develops and de- oys high-speed services. Cable opera- rs already have placed big orders with ich manufacturers as Motorola, Toshiba, ewlett-Packard, and Intel.

LORIOUS SCENARIO." To offer cable- odem service, operators must fortify eir networks with lots of optical fiber, hile equipping the coaxial cable por- on with new amplifiers that work in oth directions, upstream and down- ream. But the operators are making at investment anyway by spending ughly $1.5 billion a year to increase hannel capacity and signal quality, and et the stage for interactive TV. Robert . Luff, chief technical officer for broad- and at equipment supplier Scientific- tlanta Inc., estimates that networks apable of handling two-way cable odems could pass 40% or more of J.S. homes by 1998 and more than 0% by 2000. First to be wired, of ourse, will be the upscale neighbor- oods that are most likely to sign up or high-speed data connections.

Rivals to the cable operators are tak- ng advantage of the lull before cable nodems hit big. Hughes's DirecPC service ays it has orders for thousands of dish- s, which can't double as satellite-TV re- eivers. Its best hunting grounds: rural reas with poor cable and phone service.

Meanwhile, phone companies are sell- ng the heck out of ISDN, which con- erts standard analog phone lines into aster digital ones. Pacific Telesis Group ays ISDN is its primary approach to roviding high-bandwidth connections o the home for the near term. And Nynex Corp. recently predicted it would install 1 million ISDN lines in its erritory by 2000. In addition to reach- ng the market ahead of cable modems, ISDN can handle phone calls and two- way videoconferencing, which cable modems are ill-equipped for. And as for data, the hope is that "they're going to see pretty good performance from ISDN, and they may not see as much of a need to upgrade," says Raymond

FOR NET SURFERS WHO WANT TO POWER UP NOW

Crawling around the World Wide Web with a 14.4-kilobit-per-second modem can seem like cruising the freeway on a tricycle. You can check out nifty sites and sounds, all right, provided you haven't died of boredom first. Graduating to a state-of-the-art—and at $200, affordable—28.8-kbps modem surely helps, but you still may get the feeling that the Internet is passing you by.

Luckily, help is on the way for those with a need for speed. Cable modems will start to turn up in a few markets this year, and manufacturers are revving up speeds on conventional modems to 33.6 kbps. But for Web surfers who crave swift and immediate access to the Internet, the best bet may be via ISDN, or integrated services digital network. Data can be zipped through these digital lines at speeds of up to 128,000 bits per second—provided you have gear that can "bond" two separate channels of 64,000 bps—or roughly four times faster than a 28.8-kbps modem.

WHAT YOU'LL NEED FOR SPEED

Typical ISDN setup

LINE INSTALLATION
$135 to $200

MONTHLY FEE
$21 to $60

CONNECTION GEAR
$300 to $650

DATA: YANKEE GROUP INC.

While ISDN has existed for well over a decade, only recently have the Baby Bells pushed the service in a big way. According to Forrester Research Inc., there will be 1.5 million residential ISDN lines used for online access in 1996, up from 250,000 last year.

HOOKUP HEADACHES. But ISDN could cause you installation migraines. There are several ways to implement ISDN, so you will have to install hardware that meshes with the type of service offered by your phone company. The Bells and equipment makers have recently agreed to market four standard ISDN configurations. But "ISDN is not quite plug-and-play yet," says Vern Mackall, a senior analyst at Northern Business Information, a unit of BUSINESS WEEK's parent, The McGraw-Hill Companies. For starters, you will need a compatible modem-like device known as a terminal adapter, sold by the likes of Motorola Inc. and U.S. Robotics Corp., as well as a black box that connects to the phone company called an NT1, or network termination device.

Moreover, you typically will have to fork over a one-time installation fee to your phone company, and customers who live far away from the central office switch may pay more. U S West Inc. charges $110 if you live within 18,000 feet of the central office and an additional $100 if you live farther out. Southwestern Bell Corp. normally charges from $400 to $485 to install ISDN but will waive the fee for anyone who agrees to keep the service at least two years.

Monthly rates vary widely and may involve a per-minute charge. In Missouri, Southwestern Bell has a plan through which ISDN customers pay $45.50 per month for 10 hours of usage, plus 4¢ per minute thereafter. A different Southwestern package costs $63.50 per month and includes 80 hours of usage, after which it's 2¢ per minute. Costs vary by state: Both U S West and Pacific Bell took some heat recently over proposed rate hikes in certain markets. Pacific Bell wants to charge residential subscribers who have been paying for unmetered ISDN evening service an hourly rate during the weekend—to prevent them from dialing up an ISDN line on Friday night and staying connected until Monday morning.

Beyond cost worries, if you can't get ISDN to work properly, you might not know where to turn. Your phone company may blame the modem maker, who in turn may blame the Internet access provider (though not all Net providers or online services can handle ISDN). To smooth the way, many phone companies have formed alliances with equipment partners. Yet despite the hassles, once you've cruised cyberspace in the fast lane, there may be no slowing down.

By Edward C. Baig in New York

F. Albers, Bell Atlantic Corp.'s vice-president for technology planning.

But if "pretty good" isn't good enough, cable modems look like a better answer. Even if ISDN's two 64-kilobit channels are bonded together, their combined rate is less than one-tenth the speed of a 4-megabit cable modem. And that's the floor for cable modems: Canada's Rogers Cablesystems Ltd. is seeking suppliers of models rated at a screaming 27 megabits per second. Zenith Electronics Corp. is talking about a 40-megabit version.

ISDN advocates like to say that cable modems can't actually deliver those speeds because the bandwidth is shared by 500 or more homes. Well, yes. If enough homes send or receive data at the same time, the network would slow down. But cable executives say it then would be financially worthwhile to add fiber to cut down the number of homes sharing a network segment. Says Time Warner's Vecchi: "That would be the most glorious scenario that we could think of: All those people out there clamoring for more bandwidth."

SCARY OPTION. The cable industry could still screw things up. One hurdle comes on Apr. 15, the industry's self-imposed deadline for coming up with the rudiments of a standard so any manufacturer's modem can be used on any operator's system. If negotiators come to be at loggerheads, they could stall the growth of cable modems the way ISDN was stalled for a decade by equipment incompatibilities. What's more, the cable industry must offer reliable service, especially for telecommuters whose jobs depend on their computer hookups. Asks Tom Bayless, director of ISDN for Pacific Bell: "Are you going to bank your business on a cable company?"

Cable operators insist this opportunity is just too good to blow. At December's Western Cable Show, Comcast Corp. President Brian L. Roberts called cable modems "one of the most significant developments in the history of our industry." Indeed, cable executives worry that phone companies will draw the same conclusion and start building coaxial cable into their own networks to offer speedier services. That, rather than ISDN, may be the phone-company option that most scares the cable industry. Pacific Bell is planning a small trial of cable modems in the San Francisco Bay area. Admits Pac Bell's Bayless: "If all you care about is fast Internet access, it's probably not a bad deal."

Whoever ends up building the Info Highway to your home PC, the days of waiting interminably for keystroke commands to be answered are coming to an end. And beware: Instant gratification will make the Net even more addictive.

By Peter Coy in New York

EDUCATION

HARD LESSONS AT FOR-PROFIT SCHOOLS

First, go only where invited, and then don't overpromise

After four stormy years, the rancorous end was almost predictable. With city police shielding them from angry parents in a packed grade-school auditorium, Baltimore's Board of School Commissioners decided on Nov. 30 to cancel the remaining year of a contract for Education Alternatives Inc. to manage or administer 12 of the city's schools.

STAYING POWER: *Students at Boston Renaissance Charter School spend one-third longer in classes than peers*

Small wonder that the board pulled the plug on one of the most ambitious experiments in private management of public education. Having promised big cost savings and rapid improvement in students' test scores, EAI, opponents charged, delivered little of either. Instead, its performance dealt a "serious blow [to] the entire for-profit education industry," crowed Heidi Steffens, senior policy analyst at the National Education Assn., a leading teachers' union that opposes turning schools over to outsiders.

Can public schools and the profit motive coexist? Certainly, EAI's report card isn't glowing: The nation's biggest school-management company lost the fight to renew its contract at a Florida school in June and still is battling Hartford over its performance-based compensation. EAI's stock now trades below 6, down from a peak of nearly 49 two years ago

Yet Americans remain frustrated with educational performance that has failed to keep pace with steady spending increases and greater demand for skills in the workplace. Many remain willing to entrust outsiders with reform. "We ought to have the courage to look further afield for help," says Louise A. Sundin, president of the Minneapolis Federation of Teachers. In Minneapo

"We should expect 7% to 12% [pretax] margins. Beyond that we run into political resistance."

s, Boston, Mesa, Ariz., and other cities, rivate managers are scoring modest uccesses in public schools. A handful of ompanies now oversee some 77,000 stuents and are quietly picking up new anagement contracts (table).

They're not making much money yet. ut they are learning, slowly, what will y. While EAI attempted in Baltimore nd Hartford to take over large chunks f the systems, competitors hope to et better results by managing inividual schools. Where EAI clashed ead-on with unions and board offiials, other companies are inviting hose key players into the process—r else avoiding conflict altogether y entering schools only where suport is strong.

ATCHY RESULTS. The biggest lesson: EAI overpromised on results. Now rivals know they have a better hance at effecting reform if contituents don't expect improvements vernight. "It is romantic to think ou can hit tough goals quickly," ays Peter Hutchinson, whose Pubic Strategies Group Inc., a St. Paul onsultancy, took over the Minneapolis system in 1993. PSG has elped redesign a curriculum, reluced disciplinary problems, made eace with teachers, and righted he system's finances. But overall cademic results have been patchy: Reading and math goals haven't been met, and the gap between grades of white students and those of minorities continues to widen.

More modest measures are also he byword of the Edison Project. Onetime media magnate Christopher Whittle originally envisioned Edison as a network of 1,000 new private schools. But when his Whittle Communications collapsed in 1994, financing for Edison evaporated. Whittle lowered his aims and now runs just four schools, with contracts in hand to manage two more next year in Dade County, Fla., and one in Colorado Springs.

Edison's strategy is still ambitious—nothing less than to redesign the public school curriculum. But Whittle says he's learned to pick his spots. "We don't go where we aren't invited," he says. Willing school districts get a program heavy on teacher training, technology, and family involvement. At Edison's Boston Renaissance Charter School, housed in a 13-story downtown building, students spend a third longer in class than peers at other city schools. A new pay plan under development likely will give teachers raises based on merit rather than seniority. And red tape is circumvented. Teacher Esterjuana Gliwinski is overjoyed by the changes: "Anything you need, within reason, you can order. There's no need to go through the bureaucracy." This year, 2,100 students applied for 630 spots.

ROOM FOR IMPROVEMENT

The leading companies in for-profit public school management

EDISON PROJECT

Chris Whittle's brainchild nearly perished in Whittle Communications' 1994 collapse. What's left runs schools, using its own curriculum, in four cities. Its aim: to more than double the number of schools under management next year.

EDUCATION ALTERNATIVES

The biggest company lost contracts in Baltimore and Dade County, Fla. Now it's abandoning big-city systems, focusing instead on small suburban and rural districts.

OMBUDSMAN EDUCATIONAL SERVICES

A niche operator, it has contracts with 150 districts in nine states to provide three hours a day of instruction at storefront sites for kids with severe disciplinary or academic problems.

PUBLIC STRATEGIES GROUP

The private St. Paul consulting company is in its third and final year managing the 82-school Minneapolis district. A several-year contract extension is expected.

SYLVAN LEARNING SYSTEMS

It made its name in testing and instructional services for companies and fee-paying students. Now it has contracts to provide reading and math tutoring at 57 public schools.

Other companies are seeking out niche opportunities. Sylvan Learning Systems Inc., which long has provided education services to corporations and through its fee-based storefront centers, now runs intensive tutorial sessions for lagging students in 57 public schools, mainly in Maryland and Illinois. Kids get chits for toys and other awards when they do well; system administrators get Sylvan's guarantee that students will pull in better grades.

Ombudsman Educational Services Ltd., meanwhile, specializes in dropouts and discipline problems, putting kids through three hours of computer-based teaching a day in spartan off-site classrooms. "These kids have the opportunity to get out of the mainstream and catch their breath," says Frederic W. Skoglund, an assistant superintendent in the 70,000-student Mesa district, one of 150 systems that pay Ombudsman $15 to $18 a day for each student. "The vast majority are able to come back [to school]."

VAST POTENTIAL. Although modest, such successes likely will help break down resistance to for-profit school management. As that happens, capital could flood into an industry whose potential vastness already has captivated Wall Street. Lehman Brothers Inc. has a team of analysts and investment bankers studying the industry. Donaldson Lufkin Jenrette Inc.'s Sprout Group venture arm raised $12 million for Edison in 1994. Now, Sprout Vice-President Patrick J. Boroian thinks the business is on the verge of exploding. "This reminded us of the health-care industry 20 years ago," he says.

Investors are counting on long-term payback from the sheer volume of schools that can be turned around, but they won't likely see fat margins. Whittle warns: "we should expect 7% to 12% [pretax] margins. Beyond that we run into political resistance." He expects Edison to move into the black by 1998, after losing $6 million this year on revenue of $12 million. Meanwhile, PSG has yet to make money, though it has earned two-thirds of the pay possible under its performance-based Minneapolis contract.

EAI, which lost $7.4 million on $213.6 million in sales for the fiscal year ended last June, has a new lesson plan. "Perhaps we sold ourselves to the wrong prospective users—large, highly political, and heavily unionized districts," says Chairman John T. Golle. Now he is pursuing schools in Washington, D.C., but he also wants contracts in suburbs or rural areas such as Wappingers Falls, N.Y., and Hillsboro, N.H. He likely won't find any less contention there, though. Wherever there are parents, teachers, and politicians, passions run high—and progress, even for the profit-motivated, is bound to be slow.

By Richard A. Melcher in Minneapolis, with Mark Maremont in Boston, Roy Furchgott in Baltimore, and bureau reports

EDITED BY AMY DUNKIN

'TIS THE SEASON TO SHED SOME POUNDS

HEALTH

Resolutions to lose weight are as much a New Year's tradition as popping corks and flying confetti. And this year, because of stricter weight guidelines for adults released on Jan. 1 by the Agriculture Dept. and Health & Human Services Dept., more people than ever may realize they need to shed pounds.

Unfortunately for baby boomers, the new chart no longer allows a person to put on 15 lb. to 20 lb. during middle age: The change reflects growing evidence indicating that adding a pound or two a year after 18—as most people do—increases the risk of premature death from heart disease, diabetes, and certain cancers. "It's not O. K. to gain weight as you get older anymore," says Dr. George Blackburn, chief of the Center for the Study of Nutrition Medicine at New England Deaconess Hospital in Boston.

FRUIT AND VEGGIE. Whether you are trying to fall in line with the revised guidelines or keep a New Year's resolution, the best way to start a weight-loss program is to set reasonable goals. Nutrition experts agree that when people establish small, attainable objectives—to reduce by five pounds in a month, for example—they are more likely to achieve them and set new ones. Larger amounts may seem insurmountable and lead to a "to-hell-with-it" attitude, Blackburn says.

Also, it's helpful to view losing weight as a move toward good health rather than good looks, according to Dr. Louis Aronne, director of the Comprehensive Weight Control Center at New York Hospital and the author of *Weigh Less, Live Longer* ($22.95, John Wiley & Sons). "Progress can be measured by just feeling better or lowering your blood-pressure and blood-sugar levels," he says.

The best diets are those that feature plant foods—with animal protein and fat making occasional guest appearances. This means grocery shopping mainly in the produce department and in the bakery aisle—for whole-grain breads. Meats and dairy products should be thought of as condiments, like relish, and should be eaten accordingly. If a half-pound of relish is too much to season a meal, then so is a half-pound of hamburger.

Above all, eat a variety of foods, says Adam Drewnowski, professor and director of the Human Nutrition Program at the University of Michigan. Variety is important because it exposes the body to a wider range of macro nutrients (protein, carbohydrates) and micro ones (vitamins, minerals), which the body needs to function at its best.

BINGE-PRONE? Also, eating the same thing all the time is not exactly a palate-pleaser. "Consuming food should be satisfying," says Drewnowski. "If all you eat is broccoli, rice, and shredded carrots, for heaven's sake, go out and eat a hamburger and have a milk shake." Studies show that people who observe extremely strict diets are prone to binge eating and are more likely to abuse alcohol, drugs, and cigarettes. "The message is that if your diet doesn't have enough variety to include those things you like, you will pay a psychological price," Drewnowski says.

Of course, fatty treats such as burgers and shakes should be enjoyed in moderation. Fat has the highest calorie count per unit of any food component, and it converts to body fat most easily. Since the trick to losing weight is to burn more calories than you consume, cutting the fat helps. Here are some easy ways to eliminate unnecessary fat: In recipes for baked goods that call for oil or shortening, substitute applesauce or dried-fruit purees steeped in orange juice. Use defatted chicken broth in place of butter on vegetables. And rinse cooked ground beef in a colander before throwing it into casseroles or spaghetti sauce.

Just realize, however, that "fat-free" doesn't mean calorie-free—especially when it comes to packaged foods. "Most fat-free and reduced-fat products are full of sugar and fillers that drive the calories up almost as high as they would be if the product had the fat," warns Deanna Montgomery, assistant professor of biological sciences and nutrition at the University of Texas School of Public Health in Houston. Indeed, Nabisco's

The New Weight Guidelines

Height	Weight*	Height	Weight*
5'0"	97-128	5'9"	129-169
5'1"	101-132	5'10"	132-174
5'2"	104-137	5'11"	136-179
5'3"	107-141	6'0"	140-184
5'4"	111-146	6'1"	144-189
5'5"	114-150	6'2"	148-195
5'6"	118-155		
5'7"	121-160		
5'8"	125-164		

* The range covers women and men

DATA: U.S. AGRICULTURE DEPT

at Free Fig Newtons and ow Fat Honey Maid Gra- am Crackers, Keebler's Re- uced Fat Fudge Stripes, and other's Fat Free Fig Bars l have more sugar and total rbohydrates than their full- t counterparts. Not only es this bring their calorie unt up to within 10 to 30 lories of full-fat levels but so their higher carbohy- rate content may increase a erson's appetite.

ATER EVERYWHERE. Dr. enise Bruner, a weight-loss pecialist practicing in Ar- ngton, Va., explains that the ody releases insulin, which is a known appetite stimulant," o break down carbohydrates. hus, the higher a food's car- ohydrate count, the more in- ulin rushes into the blood- tream and the hungrier a erson may feel. Bruner says he eats only protein and uit for breakfast because carbohydrates like cereal or bagel will make me hungry gain almost before I can get o work." So she recom- ends, for their morning epast, that her patients eat ow-fat cheese, yogurt, or egg-white omelets along with a little fruit. Such high-protein, low-carbohydrate meals "don't stimulate the production of insulin" and are more likely to keep appetites in check until lunch.

Drinking water—before or between meals—can also reduce hunger pangs. Downing eight 8-oz. glasses of water a day makes for a sense of fullness and flushes out bodily wastes, including the byproducts from the breakdown of fat. "If those by-products are not cleaned out of the system, the body slows down the rate at which it burns fat," Bruner says. Without water to wash it away, fat languishes in tummies and thighs longer.

Behavioral strategies help dieters as well. Nutrition experts say it's best to avoid eating when emotionally out of sorts. New York Hospital's Aronne says extreme stress, boredom, happiness, or sadness can prompt overeating. He tells patients to "be aware of their state of mind" and to try not to eat when feelings could cloud their stomach's satiety. Other behavioral tactics include putting utensils down between bites and placing food on plates rather than eating out of pots, pans, or cartons.

One of the most effective strategies is to make a record of every crumb eaten over the course of the day. Says the University of Texas' Montgomery: "People who keep records are genuinely amazed at how much they eat and usually recognize areas where they can scale back." Several software programs, such as Parson Technology's Diet Analyst ($29) and Nutrition Expert by Fitness Software Systems ($60), are available to help track food consumption. Most computerized nutrition packages not only chronicle every morsel swallowed but also tally and graphically display a person's daily intake of calories, fat, cholesterol, sodium, and amino acids, along with vitamins and minerals.

Finding Substitutes for the Fat

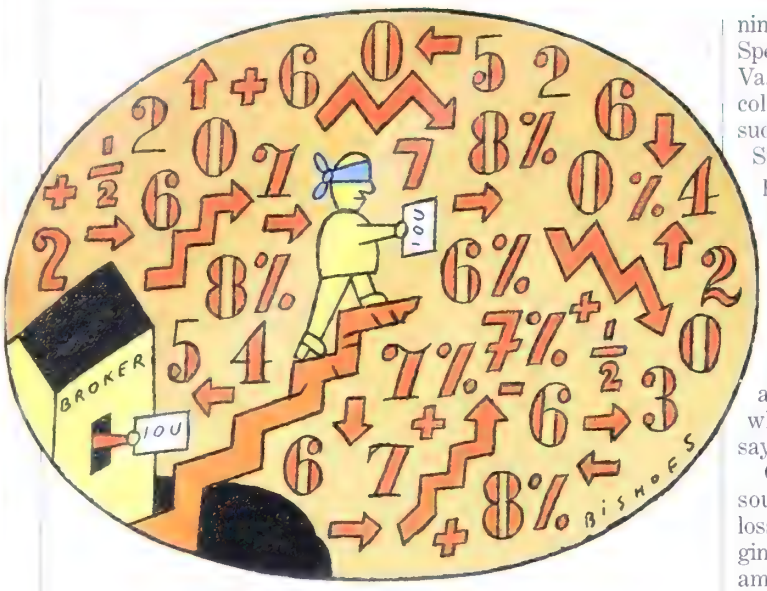
HIGH-FAT FOOD	ALTERNATIVE
BAKING CHOCOLATE	Cocoa or carob powder mixed with light oil.
BUTTER OR SHORTENING	Nonfat yogurt or sour cream blended with light oil such as canola, skimmed chicken broth (for vegetables), applesauce (for baking).
CREAM CHEESE	Nonfat yogurt blended with part-skim ricotta or cottage cheeses. (Low-fat buttermilk can be used as a thinning agent.)
MAYONNAISE	Nonfat yogurt and sour cream whipped with vinegar and egg white.
OIL-BASED DRESSINGS AND MARINADES	Mustard, vinegar, chili sauce, nonfat yogurt or whipped cottage cheese and nonfat buttermilk with herbs, pureed pickled vegetables.

DATA: BUSINESS WEEK

GROCERY LIST. Introducing a little organization into meal preparation never hurt a dieter, either. "People plan just about every other aspect of their lives but don't plan what they are going to eat," Montgomery says. Meal planning ensures that healthy ingredients are on hand to prepare that low-fat, high-fiber dinner at the end of a long day when a bag of Oreos might seem easier than a trip to the market.

Finally—exercise, exercise, exercise. Physical activity burns calories, which is, after all, the name of the game. But exercising does not have to involve donning spandex, spastically bouncing in front of a mirror, or running mile after tedious mile on a treadmill. "Vacuuming or raking leaves could do it," Aronne says. Most health-care professionals recommend a minimum of 30 minutes of exercise three days a week. It can be 30 minutes at a stretch or even three 10-minute bouts spread out during the day.

Regardless of the method you choose, a happy, healthy New Year doesn't just happen overnight. Losing weight is a slow process, and keeping it off usually requires a lifetime commitment to improved habits of eating and exercise. But with time and resolution, weight control is a piece of (low-fat, low-calorie) cake. *Kate Murphy*



BORROWING ON MARGIN SURE LOOKS TEMPTING

With all the wealth accumulated during the prolonged bull market, margin borrowing takes on new appeal. It's a great leveraging strategy if you need quick access to cash at rates considerably lower than those on personal loans at banks. But there are obvious dangers inherent in borrowing money based on the expected performance of your portfolio.

A margin account is simply a secured loan used to buy additional securities or cover personal expenses. Brokerages will extend credit of up to 50% of the value of your stocks, mutual funds, or convertible bonds. On less-volatile government bonds, you may borrow up to 95% of the value.

DANGER AHEAD. At 8.25% to 8.75%, margin-loan rates are relatively low, compared with the 15% charged by many banks for unsecured personal loans. The minimum interest rate allowed on a margin loan is half a point above the "broker loan rate," or what banks charge brokerages to borrow money. The rate now is 7.25%, but check your newspaper frequently for changes. If the loan is used for investment purposes, you may deduct only interest that would offset your investment income. There is no deduction, however, if you borrow to buy tax-exempt securities. Consider a home-equity loan first, since the interest on up to $100,000 borrowed is fully tax-deductible. The average rate is 8.86%.

SMART MONEY

Using a margin loan means shouldering some risk. If your investments take a dive—as happened lately with tech stocks—and the equity in your account falls below 30% of its current market value, your broker will issue a margin call to pay off some of the loan. If you can't come up with the cash or additional securities to satisfy the call, your broker will liquidate assets in your portfolio—possibly at a loss.

Still, margin loans can be a low-cost way to finance short-term needs, says Gregory Sullivan, president of financial planning firm Sullivan, Bruyette, Speros & Blayney in McLean, Va. Short-term uses include college tuition payments or sudden medical costs. One of Sullivan's clients, for example, knew he would get a bonus in three months. In the meantime, he needed to pay his child's $20,000 college tuition. "Instead of disturbing his $200,000 portfolio, we took a margin loan on 10% of his account and paid it off when he got the bonus," says Sullivan.

Only investors with the resources to absorb serious losses should borrow on margin. "Anyone who has a small amount of assets or has to fully leverage themselves shouldn't use a margin loan because they have nothing to fall back on," says Richard Gemberling, senior vice-president at Smith Barney in New York. And margin loans should never be used to finance existing debt: The slightest drop in the market will push you deeper into the hole, cautions financial adviser Nancy Dunnan, author of *Dun & Bradstreet Guide To Your Investments 1996* ($18.95, HarperCollins).

There are some things you can do to minimize the risks inherent in margin loans. The first rule is to deal with a broker you know and trust. "You need someone who knows your whole financial picture and advises you accordingly," Dunnan says. When you're using a margin loan to buy additional securities, keep in mind that brokers may have an incentive to encourage trading to generate commissions.

Second, borrow less than the maximum allowed. The bigger the loan, the more likely it is that slight market fluctuations will trigger a margin call (table). Your broker should inform you if the account is approaching the margin call level but Dunnan advises monitoring the price of margined stock yourself to avoid surprises.

LESS RISK. Borrowing against more stable assets also reduces the chance of a margin call. A diversified mutual fund is likely to be less volatile than an individual stock. "You get the same benefits of leverage as borrowing against common stock but with less downside risk," says Tom Taggart, a spokesman for Charles Schwab & Co. For more information write to the New York Stock Exchange, Communications Dept., 11 Wall St., 12th floor, New York, N. Y. 10005, for a free copy of *The Margin Trading Guide.*

If you choose to borrow against your newfound stock riches, bear in mind that the 37.5% average returns of the Standard & Poor's 500 stock index in 1995 were an aberration. Historically the stock market has returned 10% to 12% a year. So Sullivan cautions his clients not to finance short-term needs based on unrealistic projections of market performance.

"Managing what you owe is as important as managing what you own," says Hal Minot, director of marketing at Merrill Lynch Credit in Jacksonville, Fla. It is especially crucial when what you owe is linked to an asset that has the capability to plunge in value overnight. *Kerry Capell*

Managing the Risk

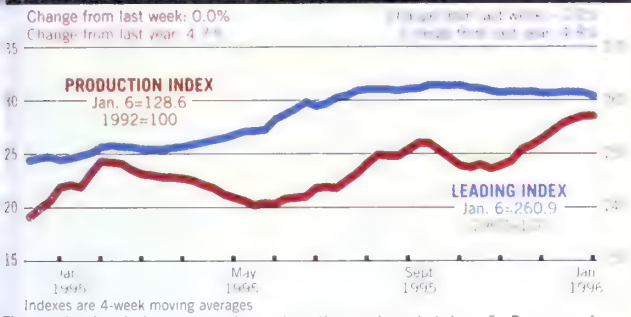
The less you borrow, the more cushion you have in a tumbling market. Using the example of 100 shares of a $60 stock, a broker can issue a margin call when you borrow:

- 50% and the share price drops to 42½, a 29% decline
- 30% and the price falls to 25¾, a 57% decline
- 10% and the price slides to 9, an 85% decrease

DATA: MERRILL LYNCH & CO.

Business Week Index

PRODUCTION AND LEADING INDEXES



Indexes are 4-week moving averages

The production index was unchanged in the week ended Jan. 6. Because of revisions to the seasonal factors in the last two weeks of 1995, the index now stands at 128.6 for Dec. 30, and 128.3 for Dec. 23. Before calculation of the four-week moving average, the index stood at 128.3 in the latest week, from 128.7 in the week of Dec. 30 and 127.6 for Dec. 23.

The leading index dropped in the latest week. The unaveraged index rose to 260.6, from 259.7.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (1/13) thous. of net tons	2,031	1,951#	0.1
AUTOS (1/13) units	91,707	78,893r#	-29.8
TRUCKS (1/13) units	[illegible]	81,322r#	-30.2
ELECTRIC POWER (1/13) millions of kilowatt-hrs.	67,271	62,656#	11.0
CRUDE-OIL REFINING (1/13) thous. of bbl./day	13,597	13,981#	-1.8
COAL (1/6) thous. of net tons	17,777#	14,785	3.3
PAPERBOARD (1/6) thous. of tons	NA#	NA	NA
PAPER (1/6) thous. of tons	NA#	NA	NA
LUMBER (1/6) millions of ft.	313.1#	213.8	-14.1
RAIL FREIGHT (1/6) billions of ton-miles	21.1#	18.4	3.4

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA[1], SFPA[2], Association of American Railroads

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (1/12) S&P 500	606.18	619.12	31.1
CORPORATE BOND YIELD, Aaa (1/12)	6.86%	6.75%	-18.9
INDUSTRIAL MATERIALS PRICES (1/12)	111.0	111.6	-2.8
BUSINESS FAILURES (1/5)	NA	603	NA
REAL ESTATE LOANS (1/3) billions	NA	$500.7	NA
MONEY SUPPLY, M2 (1/1) billions	$3,751.0	$3,748.7	4.7
INITIAL CLAIMS, UNEMPLOYMENT (12/30) thous.	NA	NA	NA

Sources: Center for International Business Cycle Research (CIBCR), Standard & Poor's, Moody's, *Journal of Commerce* (index, 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/17) $/troy oz.	397.700	400.000	4.7
STEEL SCRAP (1/16) #1 heavy, $/ton	144.50	139.50	-1.3
COPPER (1/13) ¢/lb.	121.3	126.2	-15.8
ALUMINUM (1/13) ¢/lb	77.0	79.3	-21.4
COTTON (1/13) strict low middling 1-1/16 in., ¢/lb.	81.16	80.49	-7.1
OIL (1/16) $/bbl.	18.14	19.95	-1.1

Sources: London Wednesday final setting, Chicago market, [illegible] market, NYMEX

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (1/16)	5.84%	5.28%	5.45%
COMMERCIAL PAPER (1/17) 3-month	5.41	5.45	6.17
CERTIFICATES OF DEPOSIT (1/17) 3-month	5.39	5.44	6.22
FIXED MORTGAGE (1/12) 30-year	7.37	7.30	9.35
ADJUSTABLE MORTGAGE (1/12) one-year	5.50	5.56	6.88
PRIME (1/17)	8.50	8.50	8.50

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/17)	105.42	105.21	99.28
GERMAN MARK (1/17)	1.46	1.44	1.51
BRITISH POUND (1/17)	1.53	1.55	1.59
FRENCH FRANC (1/17)	5.00	4.93	5.25
ITALIAN LIRA (1/17)	1582.3	1572.0	1595.0
CANADIAN DOLLAR (1/17)	1.37	1.36	1.42
MEXICAN PESO (1/17)	7.505	7.525	5.475

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

ERSONAL INCOME

uesday, Jan. 23, 8:30 a.m. ▶ Personal ncome probably rose 0.5% in October and .3% in November. That was the median orecast of economists surveyed by MMS nternational. Income rose 0.4% in Sep- ember. Consumer spending was likely flat n October and up 0.6% in November. hat's suggested by the monthly changes in etail sales. Spending edged up 0.2% in eptember. The government shutdown elayed release of the income report for two nonths. In addition, the monthly report will egin to state inflation-adjusted income nd spending on a chain-weighted basis to onform with data in the gross domestic roduct release.

WHOLESALE TRADE

Tuesday, Jan. 23, 10 a.m. ▶ Though usually a second-tier data series, this report on wholesale inventories and sales in November will be scrutinized because it will be one of the first looks at the inventory adjustment process in the middle of the fourth quarter. Wholesale inventories rose a large 0.7% in October, while sales fell 0.4%.

INDUSTRIAL PRODUCTION

Wednesday, Jan. 24, 9:15 a.m. ▶ Output at the nation's factories, mines, and utilities probably rose 0.2% in December, says the MMS report. The National Association of Purchasing Management's report on industrial activity showed that output fell last month. The cold weather through much of the country, though, may have sharply pushed up utility output. Production increased 0.2% in November. Operating rates probably edged up to 83.2%, from 83.1% in November.

NEW HOME SALES

Wednesday, Jan. 24, 10 a.m. ▶ New single-family homes likely sold at an annual rate of 660,000 in November, down from a 673,000 pace in October. That's suggested by the already reported 1.7% decline in existing homes for November as well as the recent flat trend in mortgage applications to buy a home.

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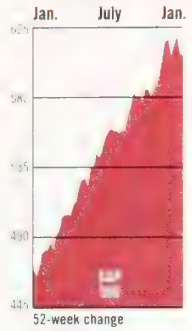
Business Week (ISSN 0007-7135) published weekly, except for one issue in January, by The McGraw-Hill Companies, Inc. Executive, Editorial, Circulation, and Advertising Offices, 1221 Avenue of the Americas, New York, N.Y. 10020. U.S. subscriber rate $49.95/year; Canada, CDN $69/year. Second-class postage paid at New York, N.Y., and at additional mailing offices. Postage paid at Montreal, P.Q. Canada Post International Publications Mail Product Sales Agreement No. 246484. Postmaster: Send address changes to BUSINESS WEEK, P.O. Box 430, Hightstown, N.J. 08520

Investment Figures of the Week

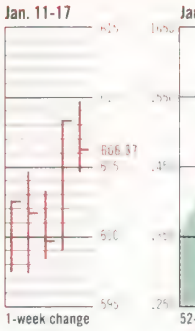
OMMENTARY

rnings ruled the U.S. stock mar- t this week. The broad averages re up slightly for the week, but dividual stocks and sectors took eir cues from earnings an- uncements. Semiconductors took on the chin, when Intel reported Jan. 16 that fourth-quarter prof- were below Street expectations. el fell 5 points, or 10%. Wal- art also reported disappointing rnings, and its stock was pum- eled, falling nearly 10%. Bank ocks, on the other hand, shone, Citicorp, Chemical, and Chase anhattan reported nifty profits.

STOCKS

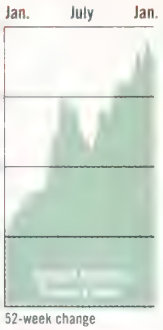


52-week change
+29.1%

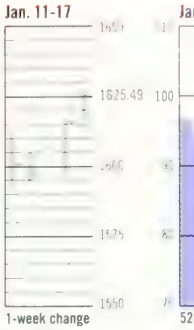


1-week change
+1.3%

BONDS

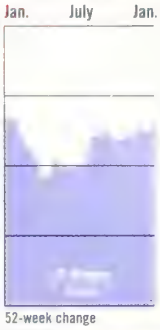


52-week change
+19.1%



1-week change
+2.0%

THE DOLLAR



52-week change
–0.8%

1-week change
+0.7%

MARKET ANALYSIS

S. STOCKS	Latest	% change Week	% change 52-week
)W JONES INDUSTRIALS	5066.9	0.7	29.0
IDSIZE COMPANIES (S&P MidCap Index)	210.4	1.0	21.2
MALL COMPANIES (Russell 2000)	302.6	–0.1	19.9
.L COMPANIES (Russell 3000)	344.7	1.3	28.0
OREIGN STOCKS	**Latest**	**% change (local currency) Week**	**% change (local currency) 52-week**
NDON (FINANCIAL TIMES 100)	3704.2	0.9	21.3
KYO (NIKKEI INDEX)	20,570.3	–0.2	7.0
RONTO (TSE COMPOSITE)	4773.0	–0.2	14.4

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.13%	5.17%	5.85%
30-YEAR TREASURY BOND YIELD	6.01%	6.19%	7.77%
S&P 500 DIVIDEND YIELD	2.27%	2.27%	2.76%
S&P 500 PRICE/EARNINGS RATIO	17.1	16.9	17.1
TECHNICAL INDICATORS	**Latest**	**Week ago**	**Reading**
S&P 500 200-day moving average	565.3	562.8	Positive
Stocks above 200-day moving average	64.0%	63.0%r	Neutral
Speculative sentiment: Put/call ratio	0.78	0.75r	Positive
Insider sentiment: Vickers sell/buy ratio	1.45	1.33	Positive

BLOOMBERG FINANCIAL MARKETS

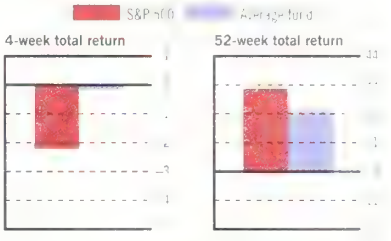
INDUSTRY GROUPS

NE-MONTH LEADERS	% change 1-month	% change 12-month	Strongest stock in group	% change 1-month	% change 12-month	Price
DEFENSE ELECTRONICS	25.8	130.9	LORAL	30.3	129.7	43 1/4
GOLD MINING	9.5	28.5	NEWMONT MINING	15.1	44.1	51 1/4
HEALTH CARE SERVICES	7.9	49.9	ALZA	19.0	29.6	27 3/8
HOSPITAL MANAGEMENT	7.2	43.6	TENET HEALTHCARE	9.2	46.9	20 1/4
ELECTRIC COMPANIES	4.4	21.9	CONSOLIDATED EDISON	11.1	23.9	33 1/4
NE-MONTH LAGGARDS	**% change 1-month**	**% change 12-month**	**Weakest stock in group**	**% change 1-month**	**% change 12-month**	**Price**
SEMICONDUCTORS	–12.6	13.1	NATIONAL SEMICONDUCTOR	–29.1	–20.6	15 7/8
ALUMINUM	–8.9	7.0	REYNOLDS METALS	–11.6	–8.0	50 7/8
TRUCKING	–8.7	–16.0	CALIBER SYSTEM	–25.6	–30.8	37 7/8
PERSONAL LOANS	–8.2	26.3	HOUSEHOLD INTERNATIONAL	–9.4	32.2	52 7/8
COMMUNICATIONS EQUIPMENT	–7.6	30.8	DSC COMMUNICATIONS	–29.6	–39.1	23 1/8

MUTUAL FUNDS

EADERS our-week total return	%
LEXINGTON STRATEGIC INVESTMENTS	18.8
WRIGHT EQUIFUND-MEXICO	16.6
MORGAN STANLEY LATIN AMERICAN A	14.9
2-week total return	**%**
ALGER CAPITAL APPRECIATION	65.1
PERKINS OPPORTUNITY	60.6
FIDELITY SELECT ELECTRONICS	58.6

LAGGARDS Four-week total return	%
FIDELITY SELECT SOFTWARE & COMPUTER	–10.2
TWENTIETH CENTURY GIFTRUST INVESTORS	–10.1
STEADMAN AMERICAN INDUSTRY	–9.8
52-week total return	**%**
STEADMAN TECHNOLOGY GROWTH	–33.1
EV MARATHON GREATER INDIA	–31.9
STEADMAN AMERICAN INDUSTRY	–27.5



RELATIVE PORTFOLIOS

Dollar amounts represent the present value of $10,000 invested one year ago in each portfolio

Percentages indicate five-day total returns

U.S. stocks	Treasury bonds	Foreign stocks	Money market fund	Gold
$13,189	**$13,066**	**$12,286**	**$10,564**	**$10,426**
–0.17%	–0.68%	–0.89%	+0.12%	+0.77%

All data on this page are as of market close Wednesday, Jan. 17, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close Jan. 16. Mutual fund returns are as of Jan. 12. Relative portfolios are valued as of Jan. 16. A more detailed explanation of this page is available on request. r=revised

GOP ROOKIES: TAKE 'YES' FOR AN ANSWER

What's with the GOP freshmen? They won't take "yes" for an answer. Elected as conservatives, pledged to enact the Contract With America, the tight-knit group of 74 Republican frosh can't seem to close the deal. Facing reelection in November, the rookies have yet to deliver on a single piece of legislation balancing the budget, reforming welfare, cutting family taxes, giving business regulatory relief, or even reforming litigation. Rather than compromise even slightly, they have closed the government, threatened the U.S. with fiscal default, and plunged in public standing.

It's a sad spectacle because the GOP freshmen have actually won the battle of the paradigm. They have succeeded in changing the national political agenda. Political discourse is now held in terms of how small a government the U.S. should have, how decentralized it should be, and how much it should cost. The freshmen have had victories in terms of broad policy as well. President Clinton succumbed to their pressure to agree to a seven-year budget-balancing deal with economic projections vetted by the nonpartisan Congressional Budget Office. Yet when key differences in the budget negotiations over Medicare, Medicaid, and tax cuts narrowed sharply between Clinton and House Speaker Gingrich on Dec. 19, the freshmen yanked Gingrich back from closing the deal. Accepting nothing less than a total win, they branded him a turncoat and insisted the government remain closed. This allowed Clinton major demagoguery of his own—claiming that Republicans were cutting Medicare, not simply trimming its growth rate.

The freshmen's unwillingness to compromise with either the Democrats or their own Senate moderates has led to a total legislative impasse. Their inflexibility, combined with a determination to gut popular environmental protection programs, has led the GOP freshmen to appear to be champions of the fringe, not the mainstream. Impractical and arrogant, the GOP freshmen are on a self-destructive course.

The result? The scorched-earth tactics of shutting down the government twice and pushing the U.S. toward default on its debt have turned off and polarized voters. The polls show that congressional Republicans have fallen into as much disfavor with the electorate as the Democrats. Newt Gingrich (R-Ga.), godfather to the freshmen class of 1994, is widely disliked, thanks, in part, to the freshmen tactics. Even some corporate CEOs are beginning to worry about GOP extremism.

The GOP freshmen's legislative ineffectuality may turn out to be less of a liability to voters in the November congressional elections than their campaign-finance hypocrisy. Despite talk about changing business-as-usual special-interest politics in Washington, no other freshman class has porked up on PAC money more than the class of 1994. While Zach Wamp (R-Tenn.) and a handful of others have refused PAC money, virtually everyone else is feeding at the trough.

The need for campaign money explains some of the positions taken by GOP freshmen, particularly those from Western states. While they have been quick to cut funding for welfare mothers and the poor, they have backed government spending for logging, mining, grazing, and farming. These same freshmen have been in the forefront of trying to defund the Clean Air Act, the Environmental Protection Agency, and the Endangered Species Act. Special interests have reciprocated by pouring millions into their campaigns. This kind of political behavior turned off voters in 1994. It may again in 1996.

The GOP freshmen have a small window of opportunity to salvage their reputation. They can start by striking a budget deal. It is by far the most significant piece of legislation on the table. The freshmen should be more practical, less ideological. Ditto for welfare, regulation, and litigation reform. This will give the freshmen a track record of success to run on and counter their current reputation for inflexibility, extremism, and an unseemly appetite for special-interest money.

CHINA'S ALARMING LEAP BACKWARD

A big chill is blowing through China. With ailing reformer Deng Xiaoping out of the picture, conservative groups are reasserting their power in Beijing. The military, allied with the Communist Party and bureaucracy, is reclaiming its authority over supporters of open markets and a more liberal political society. It may be a temporary setback. Or it may not. Business beware.

The latest crackdown from the State Council cited national security reasons in ordering Reuter, Dow Jones, and other financial-news agencies to submit to control by the state-run Xinhua News Agency. The goal is to restrict the flow of information into China, and perhaps give the news agency a piece of the growing financial information services pie.

In politics, Beijing has cracked down on religious groups as well as human-rights activists. The military is again drilling students in the virtues of the Communist Party and it has intensified its saber rattling against Taiwan. Economically, Beijing has proposed scrapping preferential tax policies for foreign companies and killed plans to reform the banking system. Piracy of U.S. intellectual property continues.

What is the West to do? It is clear that delinking trade and human rights is not turning China into an open society. But the West should continue to support the forces for economic and political change. Cowed by the military, they remain a strong and growing constituency inside China. They are also China's only hope for entry into the World Trade Organization. The current wave of heavy-handed policies emerging from Beijing can only keep China from joining the WTO at this time.

February 5

INGS

THE BEST MUTUAL FUNDS

- HIGH RETURNS, LOW RISK
- AFTERTAX PERFORMANCE
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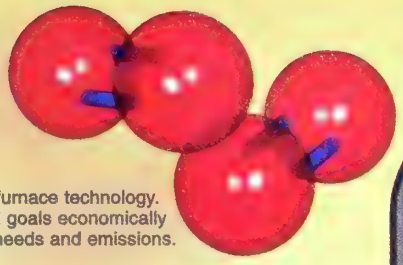

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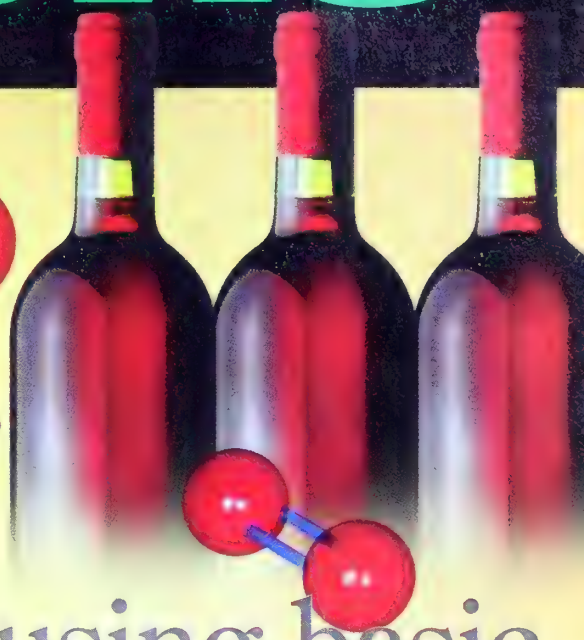

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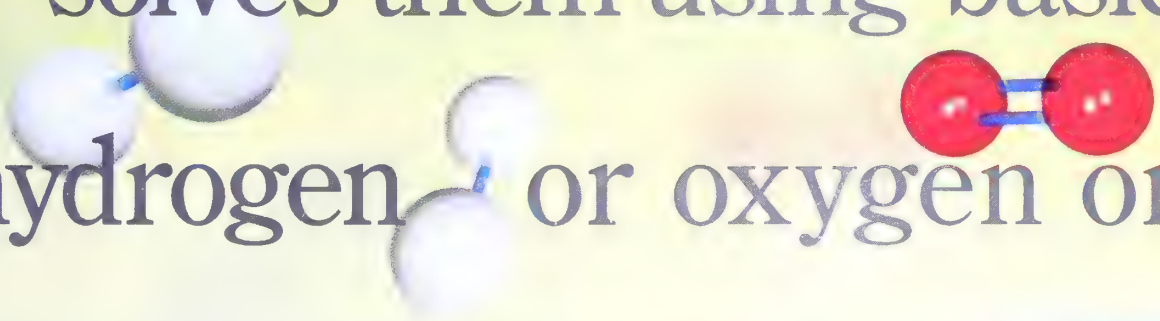

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BusinessWeek
FEBRUARY 5, 1996

COVER STORY

RUNNING SCARED

Apple set its image 12 years ago with the Mac's debut—youthful, rebellious, in your face. But its creative, anti-corporate ethos had a dark side page 34

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Apple Computer has gone from the hip flagbearer of high tech to a company losing market share, top talent, and its technology edge. Apple's renegade culture created the marvels of the Mac, but later chiefs Sculley and Spindler let Microsoft close the gap. Now, as Apple gropes for a strategy, will it opt for a partner—like Sun Microsystems—to help restore its tarnished image?

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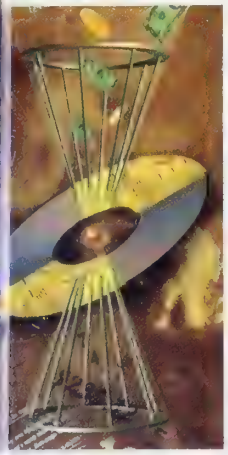

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Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

TALK SHOW "The era of big government is over. But we can't go back to the era of fending for yourself." — *President Bill Clinton, in the State of the Union*

"President Clinton may well be the rear guard of the welfare state." — *Senator Bob Dole (R-Kan.), in GOP response*

RANK AND FILE

GETTING ORGANIZED AT THE AFL-CIO

JOHN SWEENEY SWEPT INTO the AFL-CIO presidency in October, promising to revive a near-moribund labor movement. On Jan. 24, he gave the federation's executive council plans to expand shrunken union rolls, get much more involved in congressional elections, and launch a media campaign on workers' falling wages.

Historically, the AFL-CIO has left organizing largely to individual unions. Sweeney wants to spend $20 million, a fourfold increase, on the task—with nationwide multiunion membership drives and the organizing of entire regions or industries. The federation will be a national clearinghouse, dispensing tactics to the field. Sweeney also will create a department to help unions mount pressure campaigns against employers. Individual unions increasingly have scored gains with this approach, making use of ad blitzes, stockholder actions, and safety-related lawsuits.

SWEENEY: *New gambits to revive labor*

The AFL-CIO has never before tried to implement a nationally coordinated political campaign. For the Jan. 30 Senate special election to fill the Bob Packwood vacancy, Sweeney has mobilized 35 operatives in Oregon to help pro-labor Democrat Ron Wyden by trying to sway union members, many of whom vote Republican. Sweeney hopes to replicate the effort in 75 key congressional races this fall.

The media campaign on declining wages—TV, radio, print—will feature American families coping with falling living standards. Sweeney's goal: to change the nation's negative attitude toward unions. *Aaron Bernstein*

HONCHOS

IF YOU CAN FIND A BETTER VENUE . . .

IACOCCA: *Hello, L.A.*

WHERE DOES LEE Iacocca live, anyway—California or Michigan? That's a recurring question in court suits.

When Iacocca was getting divorced last spring, he got the case heard in Michigan—not California, where his wife wanted it. In California, where Darrien Iacocca claimed the couple had lived since 1992, the divorce law calls for a 50-50 asset split. But the ex-Chrysler chairman successfully argued that he really lived in a Bloomfield Hills (Mich.) condo. The divorce was later settled for undisclosed terms in Michigan, where there's no hard-and-fast divorce law on property division.

Now, Iacocca says he lives in Los Angeles. And that's where he wants his suit against Auburn Hills (Mich.)-based Chrysler heard, seeking to recoup $42 million in stock options it voided because of his ties to Kirk Kerkorian. Iacocca court filings say California case law is tough on employers who revoke compensation. Also, Iacocca says a Michigan case is inconvenient, since it would distract from his California business and civic activities. An L. A. judge has tossed out his move to hear the suit there, but Iacocca has a Feb. 28 hearing in suburban Detroit to shift venue west. *Bill Vlasic*

WILD BLUE YONDER

PILOTS TO DELTA: WE MAY WALK

DELTA AIR LINES FACES ITS first-ever pilots' strike unless negotiations turn around fast. Leaders of Delta's Air Line Pilots Assn. met in Dallas Jan. 24 to discuss mailing strike ballots to the No. 3 U.S. carrier's 8,500 pilots.

In December, things looked much better. Delta had seemingly charted a strike-free route to its targeted $340 million in pilot cost cuts, winning tentative union agreement to fly new short-haul routes at lower pay. But the union isn't backing off demands for stock and a board seat. And it has countered a Delta demand for 7% wage cuts with a proposed 5% hike based on earnings, which only returned to the black in 1995's second quarter. Delta's chief negotiator, Harry Alger, calls the proposal "a retreat from reality."

IN THE BLACK *but worried*

Adding to the pilots' ire: Company negotiators are vowing to employ nonunion pilots to protect Delta's flank in Florida if a contract is not nailed down by mid-February. "We are looking at a time-critical face-off," warns union spokesman Cam Foster. The last major pilot strike: against now-defunct Eastern in 1989. *David Greising*

THE LIST **PAVED WITH GOLD**

New York shopping districts are now even more dominant on the roster of the world's costliest areas to rent retail space. In 1994, Fifth Avenue dislodged Tokyo's Ginza, troubled by Japan's economic woes, and kept the No. 1 honor in 1995. Right behind Fifth (Tiffany, Cartier) is intersecting East 57th Street, home to showy outlets for goods that appeal more to the masses: Levi Strauss and Warner Bros.

PRIME: *Fifth and 57th*

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	STREET	(1990 RANK)	CITY	1995 AVERAGE YEARLY RETAIL*
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2	EAST 57TH STREET (FIFTH TO MADISON)	(3)	NEW YORK	440
3	THE GINZA	(1)	TOKYO	350
4	MADISON AVENUE (57TH TO 69TH ST.)	(5)	NEW YORK	300
4	POST STREET, STOCKTON STREET	(NR)	SAN FRANCISCO	300
6	CHAMPS ELYSEES	(NR)	PARIS	280

*Rent per square foot, adjusted for currency swings NR: Not ranked

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JANUS FUNDS

[$24 billion in assets]

Up Front

CHURCH AND STATE

LEAD US NOT INTO TAXATION

THESE TELEVANGELISTS DON'T want to render unto Caesar. Paul and Jan Crouch are fighting local authorities' move to tax their lucrative TV operation, saying it should be exempt because the Hendersonville (Tenn.) property is a place of worship. On the Crouches' Trinity Broadcasting Network, the most widely received religious channel in the U.S., they personally host the nightly *Praise the Lord* variety program featuring music, talk-show chat, and "testimony"—audience members' recounting of their religious experiences.

THE CROUCHES: *Gold from gospel*

Sumner County and Hendersonville, near Nashville, want the Crouches to pay $64,759 in annual property taxes for the 1,600-seat studio, arguing that it's a business enterprise. While the Crouches are appealing that decision to the state, they have agreed to pay $64,707 per year on the surrounding Trinity Music City USA, a 30-acre religious theme park.

No doubt the TV center is a moneymaker. Public filings show Trinity raked in $77 million in 1994, mostly from the phone number it flashes on the screen. But there's precedent for sparing it from taxes: In the 1980s, South Carolina officials exempted Jim and Tammy Faye Bakker's Heritage USA studio from taxes. *Bill Carey*

BANK NOTES

GENTRIFYING THE MONEY ORDER

MONEY ORDERS, long used by poor people without checking accounts, are gaining popularity and moving up the economic scale. Once sold only in urban check-cashing outlets and post offices, they are increasingly in supermarkets (A&P) and even department stores (Dillard), dispensed via sleek machines.

DEAL: *Sold in stores*

Says Argia DeLutiis, who oversees money-order vending for Jewel Food Stores: "It's surprising how many we now sell outside low-income areas."

Like a certified check, which costs around $7, a money order (75¢ to $1) is a guaranteed form of payment. Nearly half of the $90 billion in money orders last year went to pay utility bills.

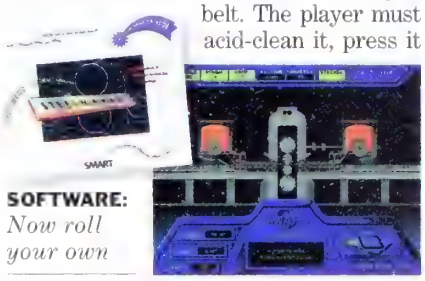
Demand is rising for money orders (5% a year), analysts say, largely because banks are cutting back on customer service and charging higher rates for certified checks. "We're glad banks are turning people away," says John Teets, chief of conglomerate Dial, which owns Travelers Express, the leading money-order outfit. You can buy a bank money order, of course, but often at double Travelers' rate. □

DRAWN & QUARTERED

PRODUCT PEEK

HOW TO MAKE STEEL WITHOUT SWEAT

EVER WANT TO RUN A STEEL mill? Well, a steel company's computer game lets you do just that, much like the Sim City game where you can build a city. Prospective Lukens customers can forge cyber-metal when the game comes out in February.



SOFTWARE: *Now roll your own*

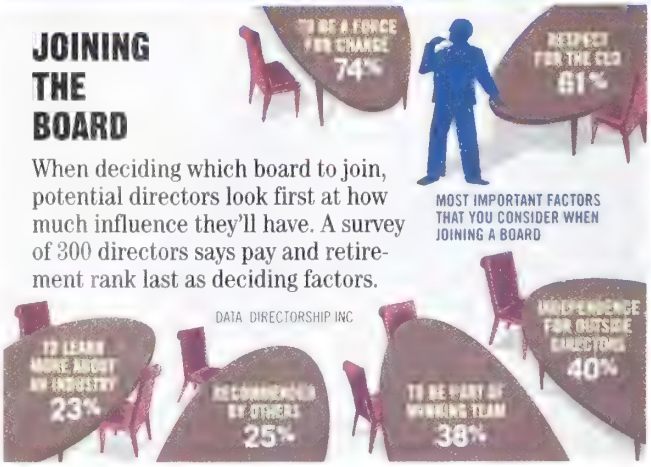
Lukens hired a software company, Virtual Creations, to produce a game based on the company's new $86 million mill in Conshohocken, Pa. The idea: spark interest in the mill and increase sales. Lukens is giving away as many as 10,000 of the $10 software kits. While music, publishing, and liquor companies have long distributed promotional software, Lukens is among the first in heavy industry to build a game around its own manufacturing process.

In *Steelmaker*, a hard-hatted steelworker delivers a custom order for a slab of steel. On screen, a red-hot slab rolls down a conveyor belt. The player must acid-clean it, press it into a thin sheet, trim the edges, coil it, and load it onto a truck—all of this through computer controls, just as steelworkers do in today's plants. Messing up is easy. Losers are dubbed "scrap-makers." *Stephen Baker*

THE BIG PICTURE

JOINING THE BOARD

When deciding which board to join, potential directors look first at how much influence they'll have. A survey of 300 directors says pay and retirement rank last as deciding factors.



FOOTNOTES Generation Xers who can't imagine retirement: 66%. Those who say leaving an inheritance is important: 81%

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Readers Report

PRO AND (MOSTLY) CON ON AL DUNLAP

It is disheartening that "The Shredder" (Cover Story, Jan. 15), on the reorganization and sale of Scott Paper Co. [to Kimberly-Clark Corp.], concentrates on laid-off workers—who are portrayed as unfortunate, hopeless, even crippled victims of restructuring. The thousands of shareholders who benefited receive little coverage. They include single mothers, widows, students saving for college, elderly stroke victims, etc. That these shareholders were able to get a very good return on their investment is an integral piece of the story.

Scott L. Barbee
Philadelphia

Dunlap appears to be the embodiment of capitalism run amok—without heart, soul, or conscience. I am especially outraged at his assertion that stakeholders are "rubbish." These are the same stakeholders that presumably constitute Scott Paper's consumer base. Dunlap eviscerated Scott Paper for short-term benefit and misled stakeholders from day one of his reign of terror about his intention for the company. This exercise in "value creation" has done little except disrupt the lives of thousands of hard-working people and cast well-deserved aspersions on the system of free enterprise.

I hope Dunlap's retirement is permanent. I believe his tenure at Scott will go down as a textbook example of management without values, management without a socially useful vision—bankrupt of new-product ideas and driven by greed. Wherever possible, I will use only the products of Scott's competitors, and I'm sure your article will prompt many others to do the same.

E. McDonnell
Summit, N.J.

We have been time-managed, benchmarked, reengineered, downsized, right-sized, and RIF'd [reduced in force]. Now, we've been "Dunlapped." From the perspective of one of those remaining, to be "Dunlapped" is to do the work that five other friends used to do, to extend the workday from 9-10 to 11-12 hours, and to receive a reduced bonus.

Richard T. Englund
Asset Engineer
Kimberly-Clark Corp.
Chester, Pa.

We'll be using the BUSINESS WEEK story in our classes to illustrate what can go wrong with corporate governance and ethics.

Joseph E. McCann
Dean, School of Business
Pacific Lutheran University
Tacoma, Wash.

OUTRAGED

"Dunlap appears to be the embodiment of capitalism run amok—without heart, soul, or conscience.... I will use only the products of Scott's competitors."

I have no respect for someone who makes money by destroying companies for profit, especially someone who does it gleefully. He is nothing but a serial corporate murderer.

Paul J. Wetor
Milwaukee

While Dunlap has certainly "cut the fat" out of Scott Paper, he has also managed to slit its throat. If "Chainsaw Al" represents the CEO of tomorrow, God help us all.

Elizabeth Hoff
St. Petersburg, Fla.

Dunlap and his six-person operating committee were absolutely brilliant as greed's Magnificent Seven. All in American business who applaud—in the name

Business Week

A publication of The McGraw-Hill Companies

FEBRUARY 5, 1996 (ISSN 0007-7135)*** 3461

Postmaster

Hightstown, N.J. 08520. Second-class postage paid at New York, N.Y., and

and Chief Executive Officer; Harold W. McGraw, III, President and Chief Operating Officer; Kenneth M. Vittor, Senior Vice President and General Counsel; Robert J. Bahash, Executive Vice President and Chief Financial Officer; Frank D. Penglase, Senior Vice President, Treasury Operations; Michael K. Hehir, President, Information Services Group.

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of investors—the actions of this unconscionable man and his buddies should enjoy watching ghouls feast on corpses.

Ray Bedingfield
President
Woodmoor Group Executive Search
Monument, Colo.

WHY COMMERCE CAN'T FIX ITS CALCULATOR

Your editorial "How not to measure the U.S. economy" (Jan. 15) begins with some understandable concerns but reaches some mistaken conclusions.

The Commerce Dept. is concerned, as you are, about the problem of measuring the changing quality of output such as software, health care, or other innovative sectors. In fact, our program to do so is the acknowledged world leader. But neither we nor anybody else has the answer. Our revision will allow analysts to make their own judgments absent definitive answers.

When we have numbers that are as reliable as the other components of gross domestic product, we'll use them. Your proposal essentially argues that we [wait to] revise GDP data when it's convenient, as opposed to under a system of objective procedures. Who determines that? Should Washington players decide when it's a good or bad time to revise the economic data? It sounds like a good idea in theory but a bad one in practice.

Everett M. Ehrlich
Under Secretary for
Economic Affairs
Commerce Dept.
Washington

THE PRINTER OF HIS DISCONTENT

As a shareholder of R. R. Donnelley & Sons Co., I read with interest your article profiling the Chicago printing house and its CEO, John R. Walter ("The press of new business," The Corporation, Jan. 15). Your readers may not be aware that missing from this report on the company that prints BUSINESS WEEK was any mention of Walter's difficulties at his scandal-plagued Metromail Corp. subsidiary.

These problems, many of which are now under investigation by the Justice Dept. and the Federal Trade Commission, relate to the questionable origin and admitted misuse of personal information about millions of Americans. One is left to wonder if the ethical and legal problems that have come to light are the result of the example the "hypercompetitive" Walter sets for his managers if return on equity is declining.

John Aristotle Phillips
President
Aristotle Publishing Inc.
Washington

Editor's note: BUSINESS WEEK did not discuss Metromail because the matter had already been widely publicized and Donnelley had taken steps to correct its problems. Donnelley says it "isn't aware" of any FTC investigation, but it understands Justice is reviewing the matter.

LET'S HEAR IT FOR LEVITT

I am greatly disturbed by your characterization of the distinguished and most decidedly effectual chairman of the Securities & Exchange Commission ("Arthur Levitt speaks softly and carries a little stick," Washington Outlook, Jan. 8). The article paints an inaccurate and mean-spirited portrait of a man who has demonstrated forceful leadership and a knack for getting the job done. Under Chairman Levitt's steady hand, the commission has accomplished goals that would not have been possible without an effective leader. His negotiating finesse has helped pave the way to reform of laws and regulations that have burdened our capital markets and our economy.

Jack Fields
Chairman
Subcommittee on
Telecommunications & Finance
Washington

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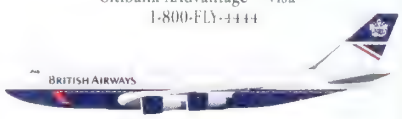

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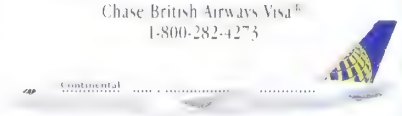

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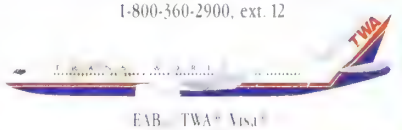

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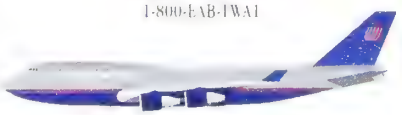

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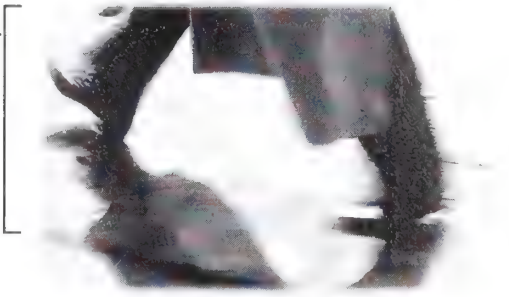
FUND	OVER-ALL	3 YR	5 YR	10 YR
FIDELITY GROWTH FUNDS				
FIDELITY BLUE CHIP GROWTH FUND	5	5	5	N/A
FIDELITY CAPITAL APPRECIATION FUND	4	5	4	N/A
FIDELITY CONTRAFUND	5	5	5	5
FIDELITY DISCIPLINED EQUITY FUND	4	4	4	N/A
FIDELITY EMERGING GROWTH FUND	5	5	N/A	N/A
FIDELITY GROWTH COMPANY FUND	5	4	4	5
FIDELITY LOW-PRICED STOCK FUND	5	5	5	N/A
FIDELITY MAGELLAN® FUND	5	4	4	5
FIDELITY MARKET INDEX FUND	4	4	4	N/A
FIDELITY OTC PORTFOLIO	5	4	4	5

FUND	OVER-ALL	3 YR	5 YR	10 YR
FIDELITY GROWTH FUNDS				
FIDELITY RETIREMENT GROWTH FUND	5	4	4	5
FIDELITY STOCK SELECTOR	5	4	5	N/A
FIDELITY VALUE FUND	4	5	4	4
FIDELITY GROWTH AND INCOME FUNDS				
FIDELITY CONVERTIBLE SECURITIES FUND	5	5	5	N/A
FIDELITY EQUITY-INCOME FUND	4	4	4	3
FIDELITY EQUITY-INCOME II FUND	5	4	5	N/A
FIDELITY FUND	4	4	4	4
FIDELITY GROWTH & INCOME PORTFOLIO	4	4	4	N/A
FIDELITY PURITAN® FUND	4	5	4	4

[1]The number of funds within the equity fund rating universe tracked by Morningstar as of 9/30/95 is 1,283, 925, and 484 on a 3-, 5-, and 10-year basis, respectively. Morningstar equity fund universe includes domestic stock funds (which include, but are not limited to, growth, growth and income, and equity income objectives), international stock funds, and specialty funds. There is a minimum 3-year performance requirement before a fund is rated.



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[2]Source: Morningstar. Data as of 9/30/95 and includes all equity and bond funds tracked by Morningstar. Top-rated funds are defined as those funds that have a 4- or 5-star overall Morningstar rating. Fidelity has 76 4- or 5-star rated funds out of 132 funds as of 9/30/95, which is more than any other fund family. Morningstar equity fund universe includes domestic stock funds (which include, but are not limited to, growth, growth and income, and equity income objectives), international stock funds, and specialty funds. Morningstar bond fund universe includes both taxable and non-taxable bond funds. [3]Morningstar proprietary ratings reflect historical risk-adjusted performance as of 9/30/95. The ratings are subject to change every month. Morningstar ratings are calculated from a fund's 3-, 5-, and 10-year average annual returns in excess of 90-day Treasury bill returns, including loads, if appropriate, and a risk factor that reflects fund performance below 3-month Treasury bill monthly returns. 35% of all funds in the equity category rate 3 stars from Morningstar. Share prices and return will vary. Fidelity Distributors Corporation.

THE GOOD LIFE AND ITS DISCONTENTS
The American Dream in the Age of Entitlement, 1945-1995
By Robert J. Samuelson
Times Books • 293pp • $25

DOWNSIZING AMERICA'S EXPECTATIONS

Although you wouldn't know it from headlines of debt defaults, Washington "train wrecks," and national paralysis, much of last fall's budget battle was a phony war. One who saw this early was *Washington Post* and *Newsweek* columnist Robert J. Samuelson, who wrote on Nov. 1 that Bill Clinton and House Speaker Newt Gingrich (R-Ga.) were in reality about a dime apart. Both knew Medicare and Medicaid had to grow more slowly. But Clinton, by resisting, saw a way to blame Republicans for heartless cuts.

Although there's no deal yet, Clinton has indeed agreed to spending cuts, while polls show the GOP got the shaft: So far, politics as usual. But as Samuelson argues in a book that richly foreshadows the budget showdown, this consensus to rein in costly programs represents a watershed for the nation.

In *The Good Life and Its Discontents*, he writes: "Something is now ending—the period in our history that began at the end of the Second World War and gave rise to a distinct vision of the American Dream." In the new era, the U.S. will begin limiting the growth of government and its promises of social improvement. Leadership, the author says, will be about lowering Americans' expectations from their government while encouraging them to shoulder more responsibilities.

This may sound suspiciously like a new Contract With America. But the compact Samuelson sees emerging is about economic choices, not dismantling Washington. Samuelson is a Big Government guy who sees today's radical conservatives, like liberal idealists of the 1970s, tugging the country back to its historic center. The problem, he argues, isn't the size of government but our exaggerated expectations of it. America is richer, stronger, more advanced, and more globally competitive than ever. But because Americans have promised themselves an unrealistic, even utopian future, they feel they're losing ground. There's mass disillusionment—at a time when the country should be congratulating itself, he maintains.

Samuelson blames a culture of government and private entitlement for this. The post-World War II generations of Americans have been taught that secure jobs, rising living standards, enlightened corporations, high-quality health care, generous government, racial harmony, a clean environment, safe cities, satisfying work, personal fulfillment, and a dominant political and economic role in the world are their birthright.

Well, maybe. But what about layoffs, low productivity, global competition, overworked and economically stretched families, guns, divorce, drugs, AIDS, racial strife, and other social ills? While these are partly to blame for a sense of things gone wrong, Samuelson sees them as misperceived.

For example, the author says that nearly the same percentage of Americans are employed in manufacturing today as in 1970, and that men 45 to 54 are actually employed with the same company longer, 12.8 years, than they were in the '60s and '70s. Layoffs do look huge, but historically they're affecting the same percentage of Americans as in the past. U.S. productivity, moreover, remains well ahead of levels in Germany and Japan.

Living standards have stagnated, he admits, and income inequality has grown. But Samuelson argues that this is due less to a decline in national prosperity than to the impact of low-paid immigrants and to the tendency of older workers, who are less likely to receive pay hikes, to keep working long past 65. Imports do destroy some manufacturing industries, but others replace them. Anyway, America's import share, 11% of gross national product, isn't big enough to reshape the overall economy.

All of these arguments are of course familiar, politically charged—and unresolvable. Samuelson, an admitted numbers addict, does his best to steer clear of ideology and partisanship and grounds his economic case with solid reporting and statistics.

But on social ills, he's much less sure. He views breakdown of the traditional family as a serious problem and sees the lack of work skills as the root cause of poverty. He doesn't view more government spending as a solution—but he doesn't have any good answers of his own, either.

Samuelson's innate caution can be frustrating. For instance, he argues that America's aging population is replacing national defense as the chief challenge facing government. But his solution for aging is to tinker. He would stretch out Social Security benefits, tax them for the wealthy, and push official retirement from 65 to 70.

Maybe that's enough. But nothing is said about whether faster growth from new technology could help pay for social problems. There's nothing on privatizing Social Security or nuking all tax loopholes with a single flat tax, or on restricting handguns, the fearsome symbol of a lawless America.

Samuelson, a Washington veteran, also reflects a common Beltway myopia: He assumes that Americans always get the government they deserve, from vast deficits to vicuña subsidies. At a time when big lobbies have already rolled over the House freshmen "reformers" and when an angry independent-party movement is building against Washington, the assumption seems unwarranted. But that's a quibble for a subject this vast and controversial. This is a smart, balanced epitaph for an era—with a few clues for what's ahead.

BY ROBERT J. DOWLING

Assistant Managing Editor Dowling was a Washington economics correspondent from 1968 to 1980.

NEW LEADERS, SAYS SAMUELSON, MUST LESSEN PEOPLE'S IDEA OF WHAT UNCLE SAM OWES THEM

BY STEPHEN H. WILDSTROM

NOW IT'S A SNAP TO SPIN A WEB SITE

New software lets you design pages without complicated programming

The World Wide Web seems to be everywhere these days. Businesses are scrambling to promote themselves on the Web. Corporations are building internal Webs to let employees share information. And just plain folks are rushing to create their "personal pages" on online services.

Until now, you needed to be half artist and half programmer to produce professional-looking pages. But this is changing, and fast. Adobe Systems Inc.'s PageMill and SiteMill (http://www.adobe.com) for the Mac could do for page design what the company's PageMaker did for desktop publishing—make it accessible to nonexperts. And with Microsoft Corp.'s Jan. 16 acquisition of Vermeer Technologies Inc. and its FrontPage Web design and management program, the computer giant (http://www.microsoft.com/msoffice/) made it clear that it will be a major player in the field.

IMAGE MAPS. PageMill is a completely visual product that lets you design your pages without complicated programming and allows you to see how they will appear on the Web while you build them. If you use Netscape Communication Corp.'s popular Navigator browser, your pages will very closely resemble what you see. Users can enter text on a page or drag it in from another application. Drop in backgrounds, graphics, clickable buttons, and blanks for entering text onto a page. And it's very simple to turn text or images into links to other Web pages. Image maps, those complex graphics where clicking on different parts of the picture takes you to different pages, are one of the Web's coolest features, but creating them has been pretty difficult. The $125 PageMill greatly simplifies the process.

Designing pages is only half the struggle of running a Web site. Keeping track of the complicated links among pages and sites—there's a reason they call it a Web—is tricky and tedious. The $400 SiteMill offers a combination of PageMill and easy-to-use tools that would be invaluable for managing even a small Web site. It provides a visual guide to how pages link to each other. And if a page is moved or renamed, SiteMill will automatically update all of the links to it. Both products are currently available only for the Mac; Windows versions are planned by midyear.

FrontPage brings a similar combination of power and simplicity to Windows (and a Mac version is in the works). While I thought the page editor wasn't as slick as PageMill, FrontPage adds one very powerful feature: Automated "WebBots" that allow a Web server to process fill-in forms and handle other common interactive chores without any programming. The main drawback to FrontPage is its $695 price tag. But I expect Microsoft will separate the editor from the site-management tools and either sell it for under $100 or incorporate it into the next release of Office.

If you want to experiment with Web page design on Windows but don't want to spend a lot of money, there are a couple of options. WebAuthor from Quarterdeck Corp. (http://www.qdeck.com/) is a $45 add-on that turns Microsoft Word 6.0 into a Web editor. InContext Corp.'s Spider (http://www.incontext.com/) is a $99 free-standing editor that is more powerful but somewhat more difficult to use. Demo versions of both can be downloaded from the Web.

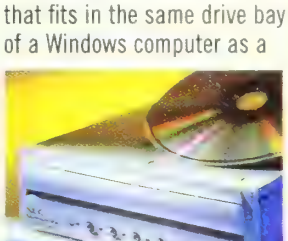
A word of warning: No matter how good your tools are, designing Web pages remains an art. Only study, practice, and some talent will make you good at it—as I learned from my own pathetic efforts. But the great software programs that are now available can speed the process greatly by letting you focus on the content while the computer worries about the mechanics.

BULLETIN BOARD

HARDWARE

A MULTIPLE CD-ROM PLAYER

I have a five-CD changer in my stereo and a six-disk unit in my car. So why should I settle for a one-disk CD-ROM in my computer? The MultiSpin 4X4 CD-ROM changer from NEC Technologies (800 632-4636) is a four-disk, quad-speed unit that fits in the same drive bay of a Windows computer as a



standard drive. And at a street price of $280, it's not much more expensive. It takes just a few seconds for the 4X4 to switch disks. The device can be tricky to configure on some computers, so you may want to pay a bit extra and have a technician install it.

THE WEB

REFERENCE TOOLS

Surfers searching for material on the World Wide Web may want to check out two new search services: Alta Vista from Digital Equipment Corp. (http://altavista.digital.com) and Excite (http://www.excite.com) from Architext Software. Alta Vista is your ticket if you want to find every reference to your search topic, no matter how obscure. Excite is much more selective. For example, a search for information on the tiny South Pacific nation of Tuvalu found eight citations, most pointing to general information about the islands. Alta Vista returned nearly 1,000 addresses, many of them with the barest connection to the island nation.

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BY PAUL CRAIG ROBERTS

REFORMS SHOULD COME FIRST– THEN BALANCE THE BUDGET

PRIORITIES: Medicare and welfare desperately need to be fixed, and not just because of their impact on federal spending

Paul Craig Roberts is John M. Olin Fellow of the Institute for Political Economy and Distinguished Fellow of the Cato Institute in Washington, D.C.

The high hopes with which the Republican Congress began 1995 have not been realized. Disunity between House and Senate Republicans contributed to the loss of momentum, but blame also lies with the GOP strategy itself.

The Republicans undertook sensitive political tasks, such as reforming Medicare and welfare, in the name of a balanced budget. The public was given little explanation for these reforms except that they were needed to balance the budget. This made it difficult for the Republicans to justify their tax proposals and easy for President Clinton to criticize the plan for callousness toward the needy and vulnerable.

The Republicans' strategy also suffers from promising a balanced budget three Congresses and two Presidencies in the future without a means of enforcing an agreement that extends beyond the term of the current Congress. Neither can the Republicans guarantee the uninterrupted seven-year economic expansion that their plan assumes. In the end, the GOP's promise of a balanced budget was less believable than Clinton's claim that people would be hurt.

SHIFT THE SPOTLIGHT. The budget stalemate provides an opportunity to gather our wits and to think about a more promising approach that would permit a balanced budget to emerge from a successful resolution of other problems.

The first point to grasp is that Clinton and Congress are fighting not over how much to cut spending and taxes but over how much to increase them. Even the Republicans' plan pumps out $339 billion more in spending by 2002 and pulls in $503 billion more in tax revenues. This strategy "cuts" taxes and spending only in the sense that it doesn't raise and spend as many additional tax revenues as Clinton prefers.

Clearing the air of budget hype would help Clinton and Congress turn their attention to necessary and unavoidable reforms. There is a bipartisan consensus that Medicare is in trouble, and Clinton himself once declared the intention to "end welfare as we know it."

The problem with Medicare is that expenditures are rising faster than the program's payroll tax base. Either we raise the payroll tax rate and accept the consequences—less employment and take-home pay—or we restrict Medicare to major medical coverage that protects against catastrophic illness. The Republicans' plan tries to achieve savings by fixing the prices of medical services, an approach that has never worked.

GROWTH AGENDA. Medicare reformed for its own sake would remove the pressure of an exploding entitlement and make it easier for a future Congress to achieve a balanced budget. Similarly for welfare: The system is widely perceived as a flop, and maintaining an open-ended entitlement that produces perverse results makes no sense regardless of the budgetary effects. Turning welfare over to the states would encourage experimentation and restraint without abandoning people in need. The case for reform should be made independently of the case for a balanced budget.

The same holds for changes in tax policy. The Republicans' conviction that tax cuts must be paid for with spending cuts is self-defeating. It not only exposes them to class-warfare rhetoric but also forecloses policy changes that would raise the economic growth rate. As former Delaware Governor Pete DuPont recently pointed out, a higher growth rate expands the tax base and is an easy way to balance the budget. An additional 0.8% in annual gross domestic product growth for five years would mean $520 billion more in government revenues.

To get these revenues, Republicans would have to build a growth agenda around their (largely abandoned) tax proposals. However, there is no sign of a growth agenda in the Republican budget, which assumes a paltry 2.3% annual growth in GDP. Among the Republican Presidential candidates, only Steve Forbes sees economic growth as a priority, and he has made it his central issue in his campaign.

The Republicans lost their growth agenda when they conceded the "fairness" issue to their opponents. If fairness is defined as using the tax system to mitigate success, then an improvement in incentives that motivates success is unfair. Thus Republicans have come up with a "fair" tax cut for taxpayers with children that is expensive and does nothing to reduce the cost of labor or capital.

It is possible that good economics might be beyond the capabilities of the political process, but the attempt to roll all reforms into a balanced-budget plan has not succeeded. It is now clear that Republicans will have to fight their policy battles one at a time.

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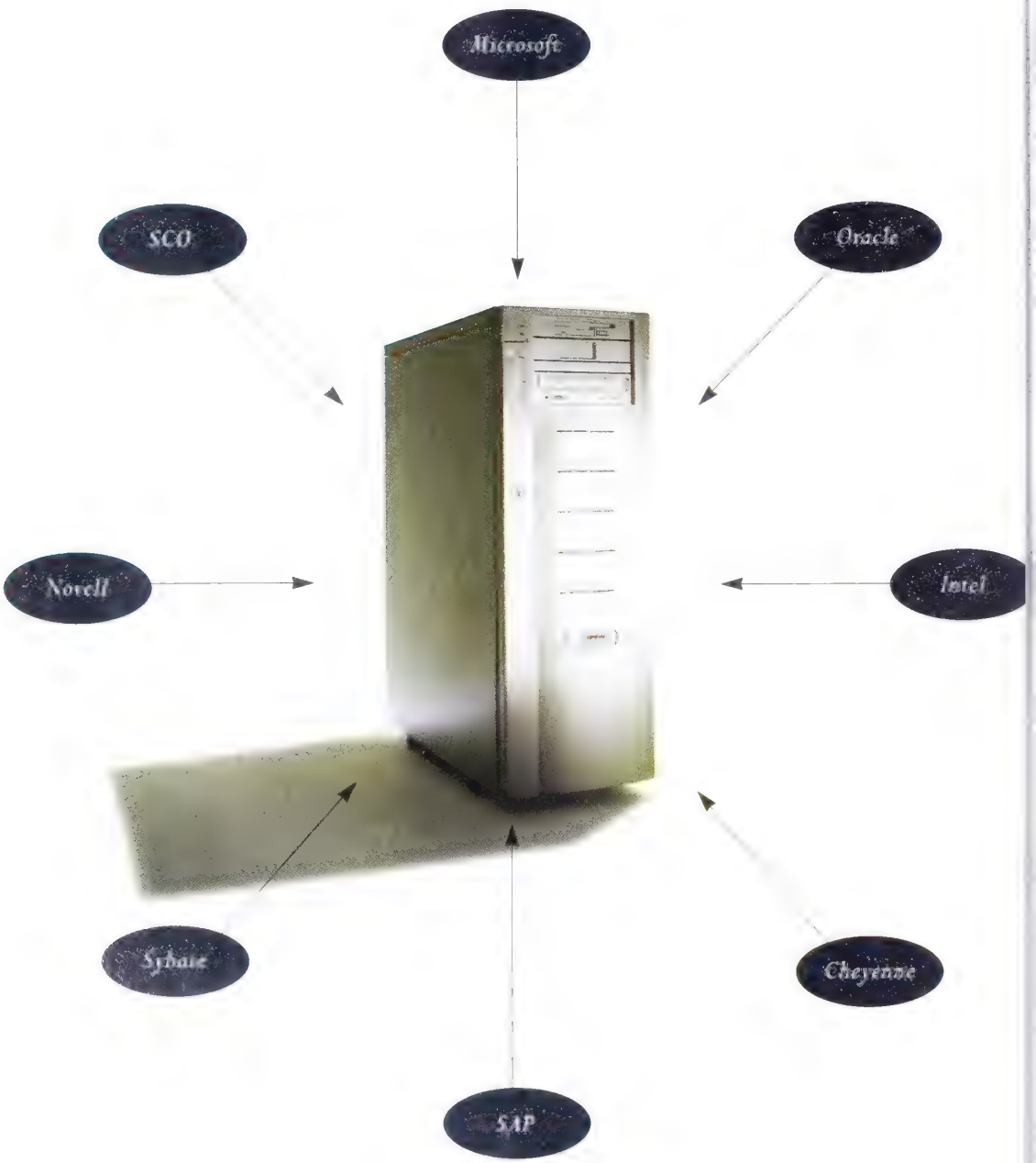

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COMPAQ

Has It Changed Your Life Yet?

BY GENE KORETZ

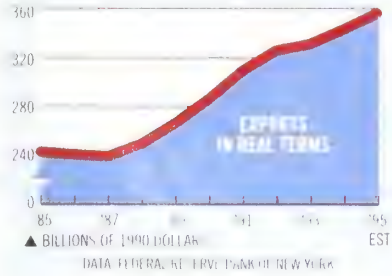
COPING WITH THE STRONG YEN

How Japanese exports hang tough

To put it mildly, Japan's trade performance in the first half of the 1990s has defied expectations. After appreciating by some 30% against the dollar from 1985 to 1990, the yen rose an additional 35% or so through 1995—enough, one might think, to cripple Japan's exports and put a huge dent in its trade surplus. Instead, Japanese exports continued to rise, while the trade surplus has shrunk only modestly.

What's behind this performance? Japanese exporters reacted to the threat of a soaring yen, reports economist Thomas Klitgaard of the Federal Reserve Bank of New York, by slashing their export prices in yen terms and cutting profit margins to the bone. From 1990 to 1995, export prices of metals, textiles, chemicals, and electrical machinery declined by 24% to 36%. Although falling costs of imported oil and raw materials helped in the price-cutting drive, so did efforts to lower wages, hold down employment, and boost productivity.

JAPAN'S EXPORTS: STILL CLIMBING



DATA: FEDERAL RESERVE BANK OF NEW YORK

At the same time, notes Klitgaard, many Japanese exporters shifted production from commodity-type goods to high-value quality products, such as luxury cars, which are less sensitive to price increases. And Japanese direct investment in nearby Asia accelerated, as manufacturers capitalized on low-cost labor abroad to turn out goods that had formerly been exported from Japan.

Thus, Japanese exports have benefited in three ways: from price-cutting, from the shift toward producing higher-value items at home, and from the surge in direct investment in Asia, which has fueled strong demand for Japanese machinery and components. Indeed, Japan's merchandise trade surplus with Asia has been running at a $60 billion annual clip.

In sum, although Japan's imports have recently been rising at a rapid rate (particularly from its factories in neighboring nations), Klitgaard notes that its exports are so much larger that its trade surplus is unlikely to shrink very much as long as Japanese exporters continue to find ways to stay competitive.

THE BLIZZARD'S BOTTOM LINE

What the storm stole from GDP

As if economists weren't already in a fog caused by the data drought during the government shutdowns, along comes the Blizzard of '96 to further obstruct their view. So how much will the winter storm's paralyzing effects dampen first-quarter economic growth?

Steven S. Roach, chief economist at Morgan Stanley & Co., has a back-of-the-envelope analysis that makes as much sense as any. He assumes that output during the week of the storm was cut in half in the areas most affected—11 states plus the District of Columbia, which represent roughly a third of the U.S. economy. Since real weekly output in a $5.5 trillion economy averages around $100 billion, one half of one third of that comes to $16 billion. Figuring that half of that is recouped by added work in subsequent weeks, Roach put the net loss caused by the blizzard at around $8 billion—enough to subtract about 0.3 percentage points from first-quarter GDP growth.

CRYSTAL BALLS WITH CATARACTS

Does age hurt forecasters' picks?

Age and wisdom are supposed to be positively correlated, if only because accumulated experience is an invaluable teacher. But in the case of economic forecasters—or rather, highly successful economic forecasters—the correlation may in fact be negative.

That, at any rate, is the implication of a new study by economist Owen Lamont of the University of Chicago. Lamont analyzed the forecasts of 15 econometric models and 118 economists whose views appeared on numerous occasions in the yearend outlook issues of BUSINESS WEEK from 1971 through 1992. Other economists have found that consensus forecasts of economic growth, inflation, and other variables are usually the most accurate.

Looking at forecasts of individuals, however, Lamont found that (unlike the econometric models surveyed) they tended to make bolder, less accurate forecasts as they aged—moving away from the consensus. Moreover, this trend was especially pronounced among the 11 forecasters surveyed who established firms bearing their own names during the 22-year period under study.

Why do independent forecasters tend to go out on shaky limbs as they age? Lamont isn't sure, but one theory is that they feel that radical predictions draw more attention than consensus views—and win them accolades on the few occasions when they come close to the mark.

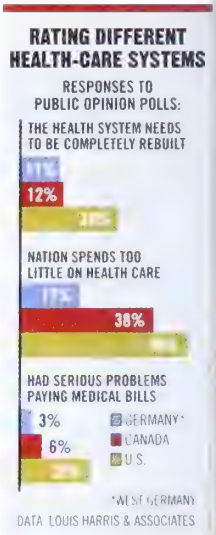
GRADING U.S. HEALTH CARE

Americans aren't all that keen

The U.S. spends over 14% of its gross domestic product on health care, more than any other nation. But as a new three-nation survey published in *Health Affairs* indicates, Americans remain far more dissatisfied with their system than Germans or Canadians.

According to the survey conducted by Louis Harris & Associates Inc. in mid-1994, only 18% of Americans compared with 30% of Germans and Canadians think their health system works pretty well. And 28% of Americans feel it needs to be completely rebuilt. At the same time, nearly half of Americans actually think their country spends too little on health care—more than in Canada and Germany. And 83% worry about too much bureaucracy in their system, a complaint shared by 74% of Canadians and just 58% of Germans.

RATING DIFFERENT HEALTH-CARE SYSTEMS



DATA: LOUIS HARRIS & ASSOCIATES

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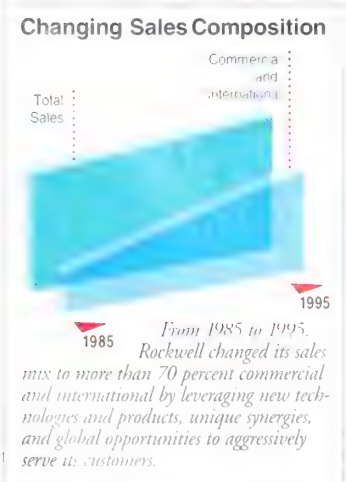

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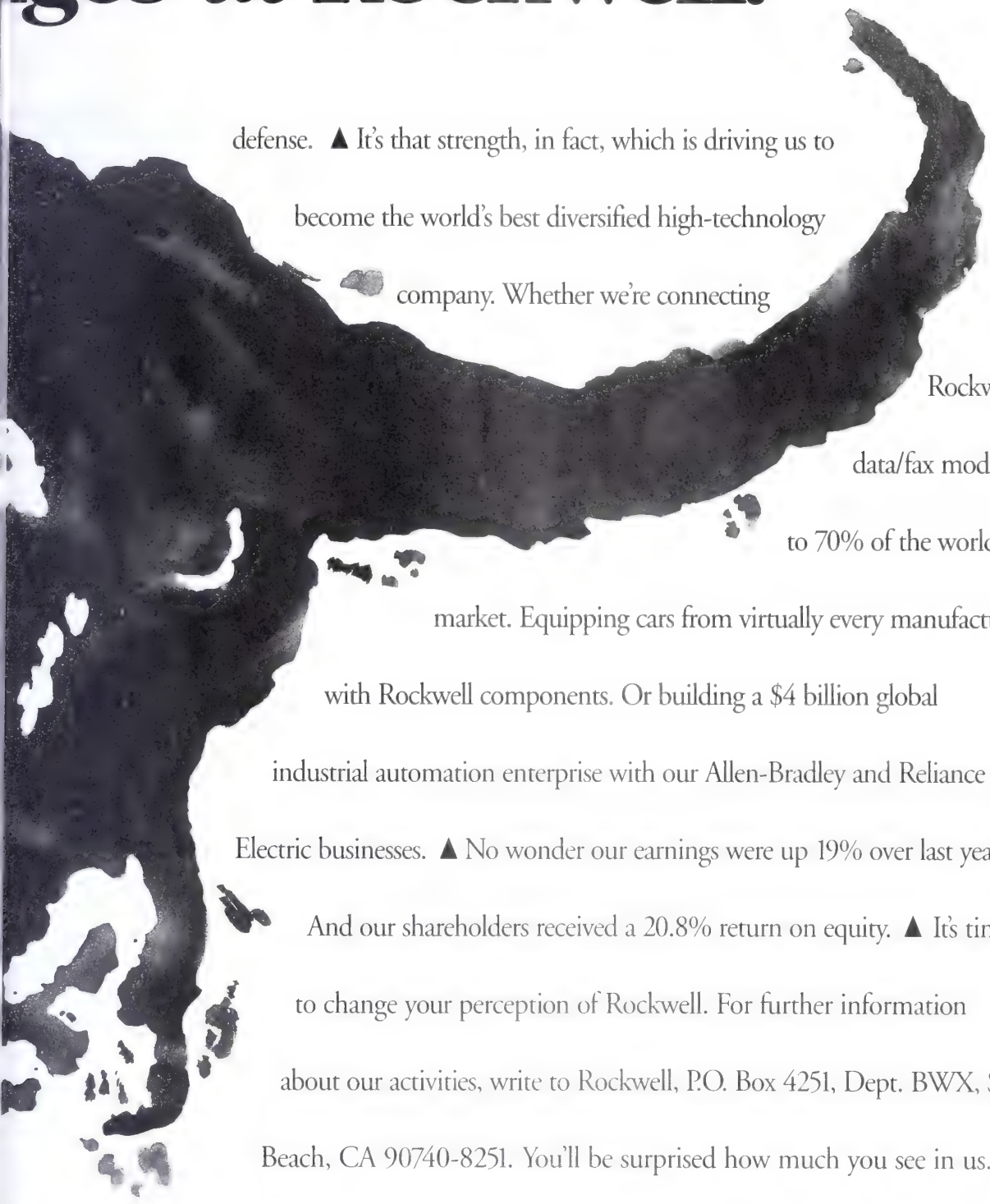

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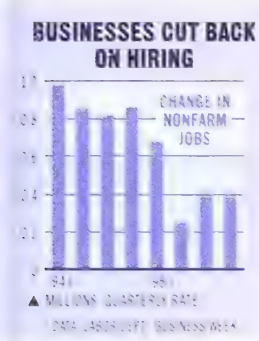
BY JAMES C. COOPER & KATHLEEN MADIGAN

HARDER EVIDENCE OF A SOFTER ECONOMY

U.S. ECONOMY With Washington's data spigots back on, economy watchers finally have new numbers to quench their thirst for information. Already, the horizon is coming into focus.

The fresh data don't change the main theme of the outlook—that growth slowed at yearend and that the softness is continuing into 1996. In fact, they go a long way toward confirming it. Reports reveal that consumers scaled back their spending in the fourth quarter and that builders were selling fewer new houses.

And in December, weaker demand caused companies to slow their hiring and cut back on work time, as businesses continued to wrestle with too much inventory. As a result, industrial production managed only a small advance in December.



The 1996 outlook also unfolds against a redesigned gross domestic product. The new chain-weighted measure of GDP shows that growth in this expansion is slower than first thought. In fact, before posting a third-quarter advance of 3.2%, the economy skated perilously close to recession in 1995's first half.

The Commerce Dept. will not report on fourth-quarter GDP until late February, but the data now coming out say that growth slowed substantially. Even so, a recession remains unlikely in 1996. The blizzard will make many January numbers look dreadful, but the economy retains enough momentum to rebound after the thaw.

THE BROADEST EVIDENCE of the fourth quarter's softness came from the Labor Dept.'s delayed employment report. Nonfarm jobs increased by 151,000 in December, on top of a 166,000 rise in November. Payrolls grew by just 383,000 last quarter, down sharply from the year-ago pace (chart). December's unemployment rate remained at 5.6%, but the labor force has barely grown in the past year.

Manufacturing jobs grew by 52,000 in December, but 31,000 of those belonged to workers returning after a strike at Boeing Co., and a further 10,000 were auto workers returning from temporary layoff. The factory workweek slipped 6 minutes, to 41.4 hours.

Weakness in manufacturing was also evident in the meager 0.1% increase in industrial production in December. The output slowdown has been especially steep during the past year (chart), and it has been broad: Output of consumer goods is flat from a year ago, and production of business equipment has slowed sharply, particularly in the fourth quarter.

Construction is not faring much better. Sales of new single-family houses fell for the fourth consecutive month in November, to an annual rate of 649,000. That drop left builders with a hefty 7.2-month supply of unsold homes—a limit on housing starts in early 1996.

Although goods producers are facing some stagnation this winter, service providers should continue their modest uptrend. Service jobs rose 85,000 in December, despite a 48,000 plunge in retailing slots. As in manufacturing, service companies reduced their average workweek by 6 minutes, to 32.6 hours.

For households, shorter workweeks mean that, even as hourly wages are starting to pull ahead of inflation, weekly paychecks are not. Nonfarm hourly wages rose 0.4% in December and were up 3.2% over the past year. That suggests that real wages are up by about 0.5% for 1995—a sign that labor markets are tightening. Yet because the workweek has shrunk, weekly pay last quarter was no higher than it was a year earlier.

That pay squeeze partly explains why consumer confidence has plateaued and why spending is wavering. The Commerce Dept. reports that real disposable income increased 0.5% in October but just 0.2% in November. At the same time, inflation-adjusted consumer purchases fell 0.6% in October and then rebounded 0.9% in November.

Assuming that strong car sales pushed up December outlays by 0.3%, real spending probably grew at an annual rate of just 1.2% last quarter—far below the rise of the second and third periods, which show the same gains under the new GDP as in the old (chart, page 32).

THE COMMERCE DEPT.'S long-awaited June 19 shift to its chain-weighted measure of real GDP went about as most economists had expected. The data, while backward-looking, nonetheless contain a couple of twists that affect the outlook.

As expected, the economy's pace is slower under the new system, mainly because the old fixed-weight measure overstated the growth of key fast-growth sec-

tors, such as computers and other high-tech equipment, where prices are falling (BW—July 31).

The new data show the annual rate of growth to be just 2.5% during the first 4½ years of this expansion—as opposed to 3.1% under the old 1987-based "fixed-weight" measure. Growth during just the past two years was lowered sharply by nearly a full point (2.7% vs. 3.6%).

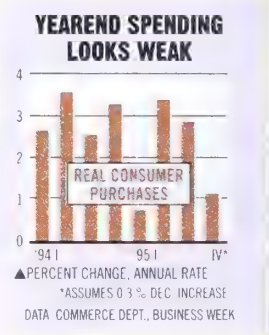
The most striking revision occurred in last year's first half, when—according to the new reckoning—the economy had a close brush with recession (first- and second-quarter growth of 0.6% and 0.5%, respectively, vs. 2.7% and 1.3%).

DETAILS IN THE GDP NUMBERS show three trends worth noting: First, an improving trade deficit accounted for a chunk of the third quarter's growth. Exports picked up, after being slowed by the nosedive in Mexican demand, and imports grew much more slowly, reflecting softer U.S. demand. Those trends will continue in 1996, although export growth will be limited by Europe's slowdown.

Second, the adjustment from overly rapid inventory growth is moving along faster than was suggested by the old data. And in the third quarter, the mix of GDP between final sales and inventory growth shows more of the former and less of the latter—a more favorable pattern for future output gains.

The problem, though, is that the fourth-quarter pullback in demand may have stymied businesses' efforts to thin out their stock levels. So output weakness in the industrial sector is likely to extend into 1996.

The final point about the new GDP is that Commerce not only revised real GDP downward but it also lowered the growth rate of nominal, or current-dollar, GDP. That's quite a surprise. In fact, during the past two years, slower nominal GDP growth accounted for nearly 40% of the downward revision in the pace of real GDP.



It means that the dollar value of overall demand in the economy has been growing even more slowly than was previously thought. That result partly explains the economy's much softer feel in recent years, especially in the eyes of struggling businesses. More important, it also suggests that monetary policy may well be tighter than the Federal Reserve had thought, increasing the chances for more interest-rate cuts.

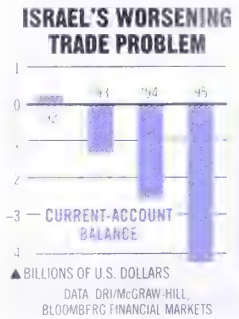
On balance, the data finally emerging from Washington tell a consistent story: The economy looked softer at yearend than it did in the third quarter—and it's going to stay that way for a while.

ISRAEL

ANOTHER FAT YEAR AHEAD

After turning in one of its best performances in years, the Israeli economy appears headed for another good year. A worsening trade position, however, replaces inflation as the major concern.

Israel's real gross domestic product grew at a healthy 6.9% in 1995, and the jobless rate slipped to 5.9% at yearend, down from 7.7% a year earlier. The benefits of the Middle East peace process and mass immigration from the former Soviet Union have helped the economy. Private forecasts expect GDP growth of between 5% and 6% in 1996.



More important, falling fruit and vegetable prices, a frozen exchange rate between the Israeli shekel and the dollar, and a tight monetary policy by the Bank of Israel cut inflation from 14.5% in 1994 to 8.1% in 1995, the lowest rate in 26 years. The government's inflation target for 1996 is a realistic range of 8% to 11%.

But the rigid exchange rate touched off a surge in imports. The current-account deficit widened to a revised $4.2 billion last year, up from $2.5 billion in 1994 (chart). The gap was first reported as $5.1 billion because the U.S. federal shutdown delayed $1.2 billion in assistance normally paid in October.

With elections due later this year, it is unlikely that the government of Prime Minister Shimon Peres will take any unpopular measures, such as a realignment of the shekel, to reduce the deficit. The elections are tentatively scheduled for October, but there is talk of an earlier date. In the meantime, Israel is paying for the deficit by increasing its foreign debt, which stands at $19 billion.

For now, Israel's low inflation and peace prospects have attracted an influx of foreign money, but the need to keep funds coming in to finance the trade gap means that interest rates will stay higher than justified by inflation. The prime rate is still a hefty 15.2%, and the central bank will continue its tight monetary policy. BOI Governor Jacob A. Frenkel has made it clear that after finally braking Israel's once rapid inflation, he has no plans to let up now.

With Neal Sandler in Jerusalem

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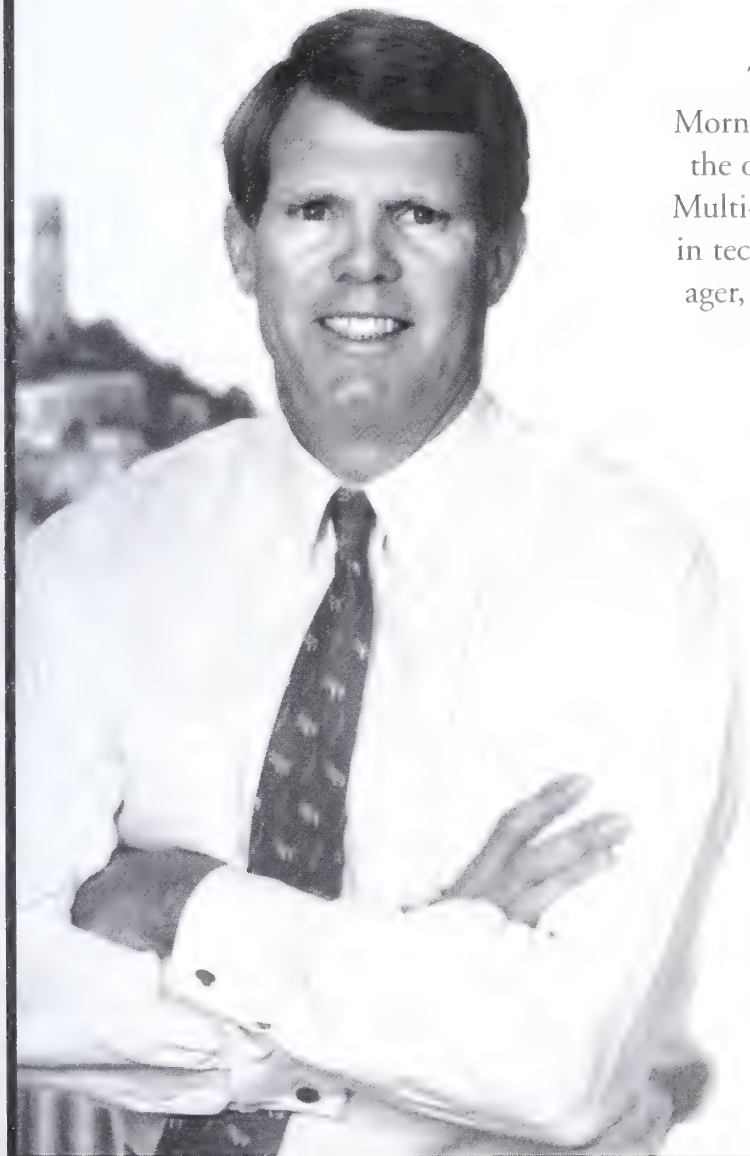

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THE FALL OF AN AMERICAN ICON

Apple Computer, once the hip flagbearer of high tech, is in sad decline. There are lessons aplenty

Cover Story

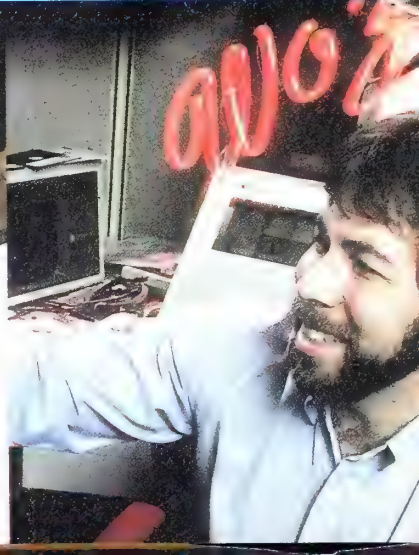
The year was 1984. Apple Computer Inc. was the Magic Kingdom. It was the hip, young heart of Silicon Valley—the place where America was showing the world how the combination of technology and entrepreneurship could make a revolution. Apple created the legend of two kids in a garage inventing a computer—and then building a New Age company where the old corporate rules were scrapped. No dress codes, no formal meetings—nothing to get in the way of what really mattered: creating computers that, Apple promised, would change the world. In a building flying a pirate flag, co-founder Steven P. Jobs had spent three years with his engineers bringing such a computer to life.

On Jan. 22, 43 million Super Bowl XVIII viewers got a glimmer of what Jobs was up to. A single 60-second commercial, which cost $1.6 million and was shown only once, crystallized the phenomenon that was Apple. The infamous Big Brother spot was a teaser for the launch of the Macintosh two days later. It showed an athlete bursting into a drab auditorium packed with corporate drones watching a figure on a huge video screen. She hurls a hammer, smashing the screen. The message: A rowdy, anti-Establishment crowd was coming to liberate Corporate America with computers for "the rest of us"—with easy-to-use graphics and a push-button mouse. It was disturbing, in-your-face. And, yes, it was the product of Apple's well-oiled image-making machine. But it captured our collective imagination.

Today, that Apple—the very icon of a post-industrial, high-tech America—is barely recognizable in the troubled $11 billion company that bears the name. Years of overlooked opportunities, flip-flop strategies, and a mind-boggling disregard for market realities have caught up with Apple. Microsoft Corp.'s Windows 95 has seriously eroded the Mac's technology edge. A belated decision to expand the Macintosh market by licensing Apple technology to other personal-computer makers has gone almost nowhere. And now, management is in near-meltdown: Out of 45 vice-presidents, 14 have been axed or left in the past year, three more are about to decamp, and CEO Michael H. Spindler's job looks threatened. Apple is rapidly becoming a minor player in the computer business and may be swallowed up by Sun Microsystems Inc. or another rival.

Already, there are signs that Apple's troubles are spooking would-be customers (page 38). In the Christmas quarter, when record numbers of shoppers snapped up computers, Mac sales

PAGES FROM APPLE'S SCRAPBOOK: *Taking corporate fitness seriously with Aikido, a four-person Macintosh team, Jobs and Sculley in 1984, hammer-throwing runner in the TV commercial that launched the Mac, Apple co-founder Wozniak, an employees' meeting in Hawaii*



A MAC LOVE AFFAIR: *Millions of customers—in offices and schools—still insist, with good reason, that the Mac*

trailed the market—even after panicky last-minute price cuts. Apple's share of the world market during the fourth quarter sank to 7.1%, down from more than 8.2% a year ago.

That doesn't mean Apple is dying. The $69 million loss in the Christmas quarter and an operating loss this quarter that analysts put at $55 million won't put much of a dent in its balance sheet, which still has $1.1 billion in cash and short-term investments. Even the layoff of 1,300 workers, about 8% of its payroll, though painful, won't match the trauma of 1985, when the company axed 20% of its workforce.

But this time, Apple has lost something it's unlikely to win back: the technology leadership that made the Macintosh so different from other computers. Millions of Apple customers still insist, with justification, that the Macintosh remains a far more elegant machine than the ordinary PC. But Microsoft has aggressively updated Windows to the point where the masses of new buyers can't see much difference between a PC and a Mac—except that the Apple machine costs more. And as Apple's poor Christmas showing demonstrates, they're not interested in paying more.

All of a sudden, the model on which Apple has built its business for more than a decade looks shaky. Its plan had depended on having enough money to fund development and marketing of new Mac technology single-handedly and pay for higher-priced components that are unique to the Mac. For most of the Mac era, Apple has been able to do this by commanding a higher price than PC clones built from Intel Corp. and Microsoft technology. Periodically, Apple has also tried another approach: bringing out cheap Macs to drive

The Jobs Era

Steve Jobs had a co-founder—Stephen Wozniak—and the venture capitalists who backed the company in 1977 immediately installed professional management. But Jobs dominated. Often brilliant, sometimes exasperatingly flaky, he imprinted Apple Computer with his distinctive, hip personality. By 1980, the company was the leading PC maker: It went public with the hottest IPO of the time, raising $96.8 million. There were fumbles, too: The Apple III office computer was a bug-infested flop. And Lisa, precursor to the Mac, was an expensive dud. Jobs's masterpiece, however, the 1984 Mac, was a stunner—with groundbreaking, easy-to-use software and a cool design. It was also severely underpowered and limited in expandability. The market balked, and in May, 1985, Jobs was pushed out of daily operations.

The Sculley Era

Handpicked by then Chairman Jobs in 1983, John Sculley brough with him two decades of marketing experience from PepsiCo. As CEO, Sculley moved quickly to remedy the Mac's shortcomings b pushing for an open design. By 1987, the product was a smash hit Apple pushed aggressively into high-profile corporate sales and expanded operations around the globe. But Apple entered the 1990s with an overpriced product line and a bloated, overperked exec tive staff. Microsoft Windows was gaining ground, and Apple's rate of innovation was slowing. Determined to catch the next technology wave, Sculley put himself in charge of research and development—and came up wit the Newton personal digital assistant, a marketing and technical fiasco. In June, 1993, the board replaced Scul ley with Michael Spindler, who had been running day-to day operations as chief operating officer.

s less frustrating to use han an ordinary PC. The handheld Newton, owever, was greeted vith ridicule in 1993

ıp market share and im- rove economies of scale. But management never tuck with that strategy— r really pushed the Mac lone business that could ıave achieved the same ends. For now, Apple is in a lose-lose ituation: It can't command top dollar or stimulate market- hare growth, even with price cuts that have slashed gross nargins from 28.7% to 15%. "The jig is really up this time," ays Chris Espinosa, a manager who has been with Apple ince 1977. "We can't do business the same way anymore."

Fearing that this day might come, Apple insiders say com- any executives began hatching a contingency plan more han a year ago: To boost Mac market share to the 20%-plus ange, they realized that they might need a powerful partner r even consider a merger. So in late 1994, Apple secretly be- gan talks to sell the company. It has approached a number of ossible suitors, including Sun Microsystems, IBM, and Hewlett-Packard. At a briefing after the Jan. 23 annual meeting—where embattled CEO Spindler had listened impassively as shareholders called for his resignation—the company told reporters that it is not for sale. Yet sources close to Sun and Apple say that some sort of deal may still be cooking.

With its stock trading at $30 and below for the first time in 18 months, Apple could be takeover bait, eliciting fresh interest from companies such as Toshiba, Canon, Motorola, and Philips, in addition to Sun. Experts figure Apple would go for about $35 a share, or $4.4 billion—about half the $8 billion that investment bankers a year ago said it might fetch. That's when Spindler approached the company most likely to pay top dollar: IBM. Now, even at a bargain price, the computer giant is no longer interested.

That leaves Sun as the most likely suitor. It could be a good fit. The workstation maker would gain Apple's office desktop business as well as Apple's Macintosh software interface for a Sun "Internet appliance"—a stripped-down PC for surfing the Net. The companies were close to a deal in December, insiders say, when Sun CEO Scott G. McNealy dropped in on Apple's board at the St. Regis Hotel in New York. The stock-swap deal would leave McNealy in charge of the combined outfit. Negotiations broke off a week later, when Apple warned of the impending quarterly loss, but they have since resumed, sources say.

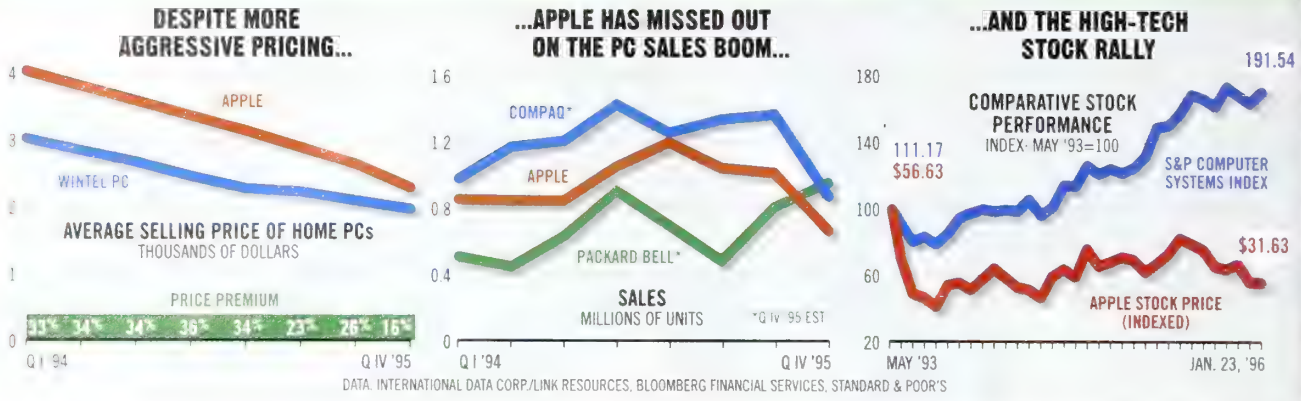
A PATTERN OF UPHEAVAL. If Apple is serious about not selling, it may wind up jettisoning assets and remaking itself into a smaller, albeit more profitable, company. It already plans to narrow its focus to market segments where it is already strong—a move that means relinquishing forever the chance of regaining the mantle of industry leader. Already, the company has hinted that it might exit the low end of the PC race. Now, its eye is on the Internet, where the company claims some technical advantages. But Apple joins a long list of Web wannabes.

How did this company—that had everything going for it—come to this sorry pass? Certainly, Spindler deserves much of the blame. During his watch, Apple's technology edge eroded dangerously. The project that could have restored that edge and countered the Windows 95 onslaught—a new Mac operating system called Copland—has fallen two

he Spindler Era

:hael Spindler started off with a 2,500-employee layoff, first move toward a new, low-margin business model. ordered up inexpensive Macs for the surging home mar- and presided over the smooth transition to a new prod- line, based on the PowerPC chip. Secretly, Apple ered into buyout talks with IBM in late 1994. Publicly, companies squabbled over a design for common PC dware built around PowerPC chips. An abrupt down- turn in Apple's fortunes came in 1995: Timid growth goals left Apple short of products. A stale PowerBook lineup halted gains in the notebook PC market, and top managers began leaving. The Christmas quarter was a disaster—even with price cuts, Mac sales were disappointing. January, 1996, brought ws of a last-quarter loss of $69 million. Laying off 1,300 rkers is just the first step in an overhaul that could lude Spindler's ouster and/or even a sale of Apple.

A Barrel of Trouble



DATA: INTERNATIONAL DATA CORP./LINK RESOURCES, BLOOMBERG FINANCIAL SERVICES, STANDARD & POOR'S

years behind schedule. And instead of moving toward his goal of doubling Mac's market share in five years, Spindler has let it shrink.

The most alarming result of Spindler's troubled tenure is the departure of many of Apple's most talented executives. Sales chief Ian Diery quit in April, and his replacement, longtime Apple exec Daniel Eilers, left last fall—both pushed out by Spindler reorganizations. In July, Frank Sanda, the charismatic leader of Apple Japan, was forced out after a strategy dispute with headquarters. Chief Financial Officer Joseph Graziano resigned in October. Apple insiders say he left after he briefed directors on what was ailing the company—specifically, Spindler's leadership. Spindler then met with the board, and when it was over, Graziano was out.

Dismal as Spindler's record is, however, Apple's woes can't all be heaped on the current boss. Nor can they be explained by the mistakes of his predecessor, John Sculley—though there were plenty of those. The fact is, despite its glowing reputation, Apple has rarely run smoothly—at least not for more than a few years at a time. There have been massive management upheavals every few years—in 1981, 1985, 1990, and 1993—and often minor ones in between. In three of those crises, A. C. "Mike" Markkula Jr., an original Apple investor and now chairman, removed the boss. For months, Apple watchers have been expecting Markkula to take out

WHY FEWER BUYERS ARE BOBBING FOR APPLES

Meet Michelle L. Whitson, Apple Computer Inc.'s worst nightmare. A real estate agent in Pinole, Calif., Whitson is the kind of consumer who has always been easy pickings for Apple. She wanted two computers: one for her husband and herself and another for her three school-age kids. After weeks of research, she decided on a Windows PC for the parents, because that's what they use at work, and a Mac for the kids, because that's what they use at school. But after Apple announced a $69 million quarterly loss and another reorganization plan on Jan. 17, she crossed Apple off her list. "I can see future directions for the PC, but I can't see it for the Mac."

For the first time, a crisis at Apple headquarters is creating a crisis of confidence in the market, and that's a terrifying situation for Apple executives. Such doubts cast a pall over Apple this past Christmas. Store shelves groaned with "Wintel" machines—PC clones based on Intel Corp. chips and running Microsoft Windows. They sported the new Mac-like Windows 95, below-Mac pricing, and the choice of a kazillion software packages. "More and more, consumers are playing it safe with the PC," says home computer analyst Andy Bose of IDC/Link in New York. "The Mac still has a certain magic, but consumers are increasingly in a Wintel state of mind." Price cuts of up to 25% in November and an army of 1,300 Mac fans deployed in stores failed to sway consumers. Worldwide PC shipments rose 25% in the fourth quarter, but Macs were up just 12%—in the U.S., a pitiful 4%. In sum, Apple took a giant step backward in the home-PC market.

WINTEL WONDERLAND. Among corporations, where flip-flopping marketing strategies long ago undermined confidence in Apple, it's getting harder for Mac lovers to hold their ground. Gary Kleinman has been the kind of customer Apple could count on. He runs an imaging lab for Walt Disney Pictures & Television and loves the Mac's multimedia powers. But now, he's looking at Microsoft Windows NT because some programs he needs aren't coming out in Mac versions. "The question never came up before," says Kleinman, "but now it has: Should we invest in Apple for the long term?"

Some of Apple's big accounts ha ready decided—against. U S West, loitte & Touche, and Electronic Da Systems are all drifting away from Mac for their desktop systems. "W want to pass data back and forth v our clients, and they have PCs," sa EDS technology consultant Norman Weizer. At Deloitte & Touche, only small pocket of graphic artists will tinue to use the Mac. "By the end next year," says Deloitte partner R Horner, "Mac use by our professio staff will be down to zero."

Corporate buyers continue to los sons for buying Macs. The latest: I longer cheaper to own one. A big s point for Apple was that despite hi sticker prices, the cost of using Ma was lower when you factored in so ware and customer support—which substantially cheaper because Mac don't need as much training. Apple ways led a Gartner Group cost-of-o ship survey. No more. At $41,439, t five-year cost of running a Mac ma Apple No. 3 behind Window NT and dows 95 PCs, according to Gartner.

How does Apple plan to reverse slide in business accounts? For star

Spindler, but on Jan. 23, Markkula again pledged his support, saying: "Michael Spindler has the full support of this board."

Until recently, Apple's gyrations hardly mattered. Rapidly growing markets and the overarching appeal of the Mac papered over almost every gaffe. But dozens of interviews with current and former executives reveal a pattern of mismanagement that caused Apple to fumble critical decisions and zigzag between strategies, bringing the company to this juncture.

The pattern began almost at the start. Back when they were helping invent the personal-computer industry with the Apple II, Jobs and co-founder Stephen Wozniak were also concocting a notoriously renegade culture. Their credo: Create your own thing, defy the naysayers, and ignore the Establishment—one person can change the world. In its finest hour, back in the building with the pirate flag, that culture brought forth the "insanely great" Mac, a groundbreaking machine whose users didn't just publish newsletters or crunch spreadsheet numbers. They fell in love.

There has always been a flip side to the Apple ethos, though. "The culture has incredibly powerful elements—Jobs's perfectionism, for one," says a former Apple executive. "But the other side of that is unharnessed and uncontrolled." Inevitably, that led to clashes between the "creators," such as Jobs and his Mac mates, and the experienced managers hired to run marketing and finance.

THE HIGH PRICE OF PEACE. The defining battle was between Jobs and Sculley, the former PepsiCo Inc. executive who was recruited in 1983 to bring depth to the management at Apple, already a billion-dollar company. Jobs, unwilling to bend his aesthetic and technical ideals to fit market realities, had made the first Mac a design statement. Dazzling to look at, it was badly underpowered and lacked the expansion capability to fix that. Within months, sales stalled, and Sculley suggested a new, more salable "open Mac." But the temperamental Jobs could not agree on how to proceed. He lobbied his board to remove Sculley. Instead, Sculley won the board over, and Jobs was ousted.

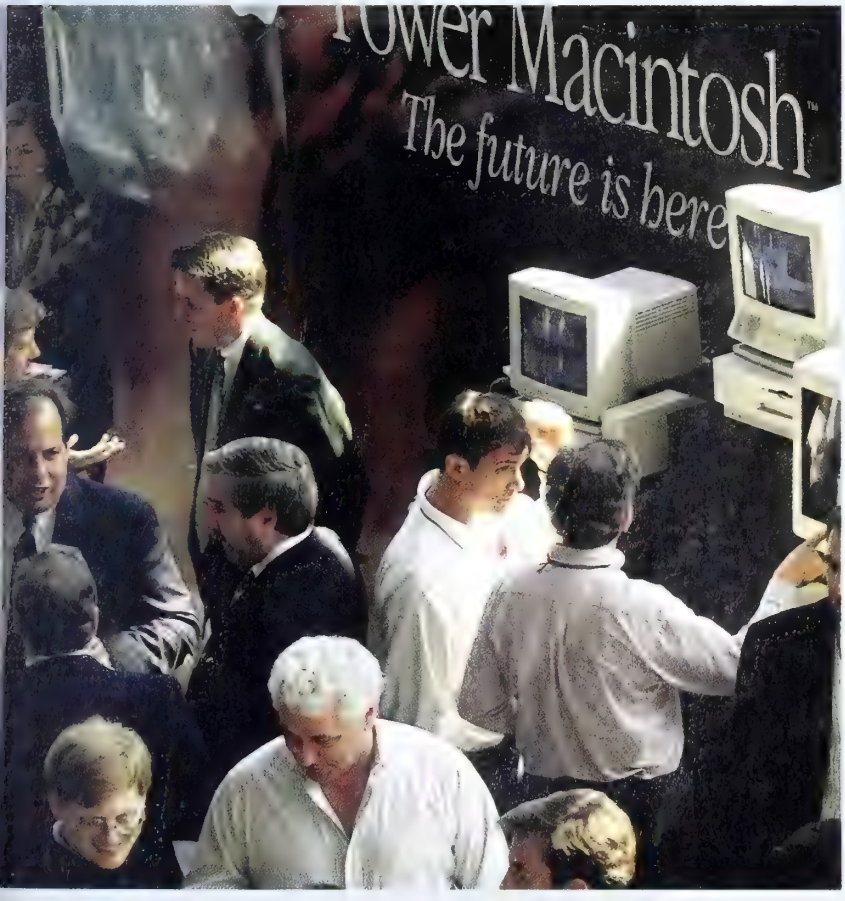
Cover Story

What happened next would help set a pattern of behavior among Apple executives that has continued ever since. As the guy who unseated Jobs and carried out sweeping layoffs, Sculley realized that he was not Mr. Popularity. He also knew that the rank and file resented the big-company systems he was putting in place. And most important, he understood that he had to keep engineers and programmers on board if Apple was to stay ahead of the technology curve. The solution was not to tinker with the culture.

It worked better than Sculley could have hoped. By 1987, the Mac was a solid hit, and with the new CEO focused on marketing, the anti-Establishment computer made inroads into Corporate America. Apple was once again a happy, if not magical, kingdom.

Nevertheless, Sculley paid a price for peace in the Apple family. By lionizing the technical "wizards" (as they described themselves on business cards), it made them tough to supervise. And his feel-good management style meant endless groping for consensus. Before long, everybody around Apple knew that a decision was rarely final. The joke began circulating that "a vote can be 15,000 to 1 and still be a tie."

That joke has gotten less funny over time. Year after year, key decisions have been postponed, reversed, or avoided completely as various executives and factions tried to push their own agendas. As far back as 1985, for instance, Apple execu-



APPLE POLISHING: *For the Power Macintosh, the future isn't what it used to be*

Apple USA President James J. Buckley says he'll get out and press the flesh. "We need to get on some planes in the next few weeks and visit our key customers." He's also going to hire new vice-presidents to focus on corporate and small-business accounts. Then there's Operation Rainbow, a plan to burnish the Apple image. "The brand is bloodred and dripping now," says Satjin Chahil, senior vice-president of marketing. "I want the rainbow back."

Even if new business customers prove hard to snag, Apple does have a constantly replenished supply of Mac zealots, thanks to its 60% share of the K-12 education market. Take 15-year-old Dan Golden of Berkeley, Calif., who lusts for a Power Mac to do homework, make videos, and do 3-D modeling of mountain bikes. He's been pushing his dad to buy a $2,200 Power Mac to replace the family's 1994 Performa. One ploy: a Power Mac picture on dad's dinner plate with a note saying "Chew On This." Would Dan consider, say, a Pentium PC instead? "Almost all my friends use the Mac, except for one girl—and she's weird, anyway." If Apple could only clone Dan.

By Peter Burrows in San Francisco, with bureau reports

"The jig is really up this time. We can't do business the same way anymore"

tives began debating the merits of licensing the Mac operating system to other computer makers—to spawn a clone industry and increase the market share for the Mac "platform." Until two years ago, however, every time top management came close to giving the go-ahead, somebody scuttled the decision.

If the clone move had been made in 1992—when a secret project known as Drama explored the notion of farming out production of a low-end Mac line to Taiwan's Acer Inc.—Apple might be in a far different position today. Says one former Apple executive: "I've never understood why somebody can't just say: 'I'm the leader. This is the way it's going to be. Thanks for the discussion, but if you don't want to do it, leave.'"

Cover Story

Such decisive leadership might have helped Apple fend off what has ultimately proved to be its nemesis: Windows. But when the first commercially successful version of the program appeared in 1990, Apple's initial reaction was dismissive. The day Windows 3.0 was launched, Apple's executive staff—including Sculley—gathered for a demo. "They were mocking it," says a former Apple manager who was there. "They said it was awkward, clumsy, a piece of junk. They were laughing. It was complete arrogance."

By this time, Sculley was focusing elsewhere. The buttoned-down East Coast executive who had made the tough decisions back in 1985 was on to a new career. No longer intimidated by Apple's gearheads, Sculley was determined to become one. After publishing his autobiography, *Odyssey*, in 1987, Sculley took on the mantle of techno-visionary.

Sculley, named chairman in 1987, anointed himself Apple's chief technology officer in 1990. He dived into the research and development labs, where he had some of Apple's best brains working on his pet project: the Newton "personal digital assistant." It was aimed at the needs of a converging computer/communications/media market. By the time Newton came out—to widespread ridicule—in 1993, Sculley said the PC business was a "cold shower" compared with the hot new markets that convergence promised.

HOLLYWOOD HOBNOBBING. Apple's board, led by Markkula, was not amused: In June, 1993, its members showed Sculley what a cold shower really feels like. According to an account in a breach-of-contract suit later filed by former corporate counsel Albert A. Eisenstat, the board—which had asked Eisenstat that spring to approach Spindler about stepping into the CEO slot—thought Sculley was ignoring day-to-day operations. He was often seen that year hobnobbing with the Clintons and politicos in Washington or with Hollywood glitterati. Caught totally off guard, Sculley was canned as CEO in a board meeting on June 17.

Spindler's emphasis on "Business 101" seemed like the long-awaited voice of reason in Apple's chaotic culture. He quickly grappled with the problems: overpriced products, sclerotic product development, and bloated costs. He laid off 2,500 workers, canned blue-sky projects, cutting R&D costs by more than $100 million a year, and flawlessly launched an entirely new product line around the speedy PowerPC microprocessor. What followed were four quarters of strong growth and a rebound in Apple's stock price—from a low of $22 to $43.

But Apple's cult of consensus and Spindler's inconsistency would prove a deadly mixture. Within a year, the hard-charging executive, who had earned the nickname Diesel in Europe, was enmeshed in a cycle of delay, reversal, and missed opportunities. Says one insider close to Spindler: "It was fine for a while. But the system converts people. People don't convert the system."

If Spindler gets the ax for Apple's dismal 1995, he can probably trace his downfall to what he did during the planning meeting for fiscal 1995. Things were looking rosy. The economy was recovering, and the new PowerPC-based Macs were in hot demand. What's more, Microsoft's "Mac killer"—Windows 95—had fallen behind schedule, giving Apple until the following August to grab market share—before the Microsoft juggernaut hit. Says an Apple executive: "We were going to make hay while the sun shined."

Then Spindler blinked. Insiders say that Ian Diery, now president of AST Research Inc., prepared a 1995 forecast of about 15% growth—the same as analysts were predicting for the industry. But CFO Graziano argued that was not aggressive enough if Apple still hoped to expand market share. The combative Diery insisted on a less ambitious agenda, according to insiders, saying the company hadn't hit its plan in years, and employees needed to "feel like they could win." A former Apple executive says: "Spindler waffled." Diery won.

When the PC market boomed, Apple couldn't keep up. Three quarters of product shortages peaked last September with what Apple said was a $1 billion backlog. Apple executives were hard-pressed to find supplies—of the Mac's custom parts and of commodities such as memory chips, disk drives, and CD-ROM drives, which all PC makers were scrambling for.

It didn't help, of course, that the boss launched a major marketing reorganization, and then reversed himself later in the year. In April, Spindler ordered up a new worldwide

KINGBREAKER: *Markkula, an early investor and now chairman, has removed Apple CEOs in past crises*

sales and marketing organization. But by November, money was tight, and Spindler pulled the plug. Instead, he ordered an all-out bid for market share. The component shortages had eased, and in November, dealers were awash in Macs. But there was a new hitch. Apple marketing execs had misread consumers: Apple had too many low-end models and too few of the powerhouses that buyers were snapping up. When the wrapping paper settled, Apple was left with $80 million worth of inventory write-offs, while IBM, Compaq Computer, and HP had cleaned up.

Another Spindler casualty has been the Mac clone business. After years of debate, he blessed a plan to license Apple's operating system to clonemakers in mid-1994. By then, Windows-based PCs were everywhere. But Apple executives insisted that they could push Mac's world market share to 20% in five years. Apple would add 1% each year and the clones the rest.

But it turned out to be a classic Apple nondecision. Even though Apple execs said they would "aggressively" pursue licensees, there was internal debate over who qualified. Insiders say that last spring, Gateway 2000 was negotiating with Apple's licensing team about cloning the Mac—but Spindler and his top executives had the final say. Sales executives, concerned that Gateway might erode rather than complement Apple's position, gave it a thumbs-down. "They just did not want to take on heavyweight competition," says an Apple executive.

And they haven't. So far, Apple has licensed the Mac design to just Pioneer, Power Computing, Umax, and Daystar. Together, they shipped about 200,000 units last year, a smidgen compared with Apple's 4.5 million. In his Jan. 17 restructuring announcement, Spindler promised "much broader" licensing initiatives. But with Apple's market share dipping, it may be a hard sell.

Perhaps Spindler's biggest misstep was botching the chance to sell Apple before its current funk. Spindler and IBM CEO Louis V. Gerstner Jr. began serious talks in September, 1994. The companies had recently collaborated with Motorola Inc. on the PowerPC chip, which was based on an old IBM chip design. Apple and IBM were both committed to using the chip in their products. In addition, the onetime rivals had thrown in their lot together against Microsoft with two software joint ventures: Kaleida Labs and Taligent—both now defunct.

Sources at both companies say Apple and IBM executives holed up for two weeks near San Francisco International Airport and hashed out what the merged company would look like. IBM would bring out a new line of PCs based on the PowerPC chip already used in Power Macs. IBM would go downmarket with its Intel-based PCs. And the two companies would use Apple's software, beefed up with IBM's OS/2, for the merged PowerPC line.

On paper, it looked good. The picture immediately dimmed when Spindler met with Gerstner near Chicago's O'Hare International Airport for a second session. As an opener, Spindler presented a golden-parachute proposal for himself and top managers. "They had written documents—a legalistic-looking wish list of compensation and severance demands," says an insider. That put Gerstner off, but IBM proceeded to offer $40 a share for Apple—and privately was willing to go as high as the mid-40s. Insiders say Spindler and Markkula rejected it as too low and suggested $60, thinking Gerstner would make a counterbid. He didn't. Talks collapsed.

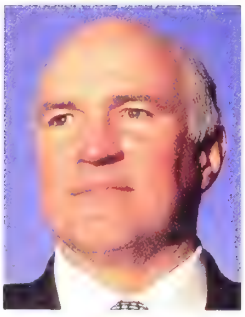
TRAILING TO THE INTERNET. In May 1995, at the urging of his board, Spindler made a second overture. Again, the chemistry was bad. Spindler "ranted and raved" for the first half-hour about how Gerstner, who was not at this meeting, had misunderstood his position in the prior go-round, say insiders. That rattled negotiators, who began to wonder if Spindler was sincere about a deal. Back in Cupertino, according to insiders, Spindler was saying in management meetings that the deal "made no sense." One former Apple exec says he concluded that "Michael wanted no part of it." Last summer, Markkula made a last-ditch attempt to pitch Apple to Gerstner. By then, however, IBM was in the middle of its $3.5 billion acquisition of Lotus Development Corp. and passed.

Then, insiders say, Apple homed in on HP and Sun. Spindler proposed a merger over dinner with Lewis E. Platt, CEO of HP, last summer. But Platt's lieutenants concluded there was no fit, given HP's thriving PC business. Regis McKenna, Apple's original public-relations man and now a consultant, approached Sun, arranging a meeting between Spindler and L. John Doerr, a Sun director. While the two companies are said to have resumed talks recently, neither company is confirming the speculation.

Can Apple help itself out of this jam? So far, investors and industry watchers are still scratching their heads. If Apple's Mac is destined never to rise to a double-digit market share,

Four Little Indians

Of 45 top execs, 14 have left Apple in the past year. Here are four high-profile casualties:



DIERY: *A victim of off-the-mark sales projections*

SANDA: *The chief of Apple Japan was ousted over strategy*

EILERS: *Forced out by one of Spindler's reorganizations*

GRAZIANO: *Had to resign as CFO after criticizing Spindler*

the company needs a radical overhaul—not the minor tune-up that Spindler laid out on Jan. 17. In the meantime, the company that once hoped to lead the world with its technology is now a follower—as the industry crowds onto the Net. "Any project that doesn't have the word Internet in it doesn't get approved anymore," says one Apple manager. Apple is selling Web servers for $3,000—that's $2,000 less than the cheapest models from Sun, Apple claims. At the Jan. 23 shareholder meeting, Spindler unveiled plans to use Newton and Pippin—a multimedia Mac player for the TV that it's licensing to others—as Internet devices.

One hopeful sign for Apple on the Net is its strong following in media and entertainment, where "content providers" are moving to the Web. "This whole Internet explosion is a real opportunity for Apple," says Eugene Wang, just-departed executive vice-president of Symantec Corp. "It's not so much an advantage for them, but it takes away some of their disadvantages." To rebound, Spindler will need to come up with some insanely great Internet products. Maybe he should rout around in the attic for that pirate flag.

By Kathy Rebello and Peter Burrows in Cupertino, Calif., and Ira Sager in New York

A BLUEPRINT FROM EUROPE?

When Marco Landi was tapped to run Apple Europe 11 months ago, he did just what some people think Apple CEO Michael H. Spindler should have done: impose discipline and accountability. "I tried to understand the Apple culture, but I didn't abide it," says the former Texas Instruments Inc. executive. "I used the good things like entrepreneurialism and innovation and tried to bring in more control and management processes."

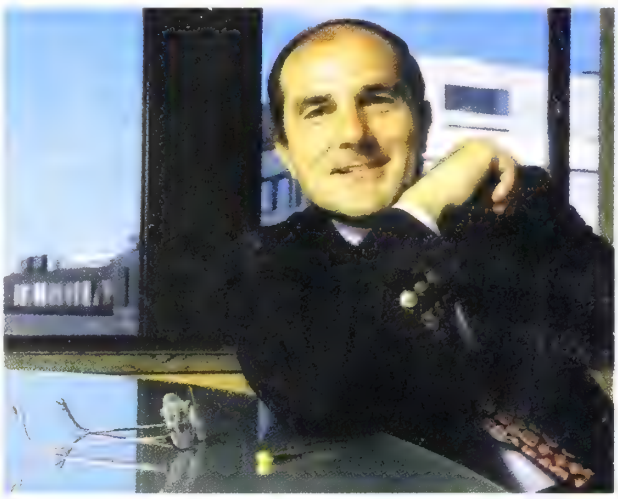
The 52-year-old Italian's overhaul of Apple Europe is producing results. While the unit lost market share for the year, Landi halted the slide in the final quarter of 1995: Sales jumped 18%, compared with an estimated market growth of 16%, according to researcher Dataquest Inc.

That's not where Landi made his mark, though. In fiscal 1995, he tripled profits—turning in the best performance of any Apple unit in the world. Insiders say Europe's profits jumped to $300 million on sales of $3.2 billion.

Has Landi perhaps created a blueprint for Spindler to use in his pending overhaul of operations? Insiders say Spindler, who once held Landi's job, is adopting many of the concepts Landi has implemented—above all, narrowing Apple's focus to markets such as desktop publishing and education, where the company can be profitable.

PATHFINDER. It may have taken an outsider to show Apple the way. During a 22-year career at Texas Instruments, Landi became a disciple of strict business controls. In his last 18 months at TI, he restructured the European operation and turbocharged its sputtering performance by slashing costs, shaking up management, and shifting TI's product mix away from commodity items. "He did a first-rate job at TI," says Geoffrey S. Carroll, a group manager of Electronic Data Systems Corp. in Europe. "If there's someone who can focus on the basics of business, it's Landi."

Another trait that sets Landi apart from the traditional Apple manager is his decisiveness. At one TI meeting, Landi became convinced the company's structure wasn't working, so he tore apart European managers' old fiefdoms based on national borders on the spot and reorganized the management lines around markets and business processes, such as sales, marketing, and distribution. "People walked out of the room with new jobs," says Marc Vodovar, a TI executive who worked with Landi for eight years.



DISCIPLINE: *Landi has brought more controls to Apple's freewheeling entrepreneurialism*

In a similar shakeup last April, Landi restructured Apple Europe, reaping 20% reduction in total costs, by eliminating country-by-country management and focusing on key markets. Already, the new structure has improved Apple's delivery speed. Under the old system, Landi says Apple Europe's distribution was dogged by shipping delays from its factory in Cork, Ireland. Now, goods reach the market in two days, not two weeks.

Landi has overhauled Apple's Paris headquarters, too. To break up the entrenched corporate culture there, he replaced 7 of the 12 managers reporting to him. "Apple is more and more professional. We still have fun, but we are much more customer-oriented," says Frédéric Spagnou, an Apple Europe manager.

ALIVE AND WELL. Pushing the Apple agenda in the market isn't nearly so straightforward. Corporate customers, shaken by reports of Apple's losses and by speculation about a possible sale, are questioning the company's future. Landi's answer: Apple is alive and well—and ready to work with them in the emerging Internet market and other areas, such as multimedia publishing.

Of course, Apple Europe is still a work in progress. Recently, Landi walked into an Apple Center in Italy and was dismayed to see no posters highlighting Apple's new Internet efforts. Within a week, Landi had Internet-ready stickers slapped on every Macintosh box. "I know where I want to go, but I can't get there alone," says Landi. If his blend of charisma and rigor in management can channel the creative spirit in Europe, he may point the way toward Apple's future.

By Gail Edmondson in Paris

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THE STATE OF THE UNION

WHAT BILL DIDN'T TELL YOU

The budget mess could get a lot worse

Welcome to fiscal purgatory. Congress and the President can't agree on a balanced-budget plan. The government limps along from one temporary spending bill to the next. The nation faces another threat of default on its debt. Little wonder that the President and GOP are struggling to end the impasse.

In his Jan. 23 State of the Union address, President Clinton reached out to the GOP. "We ought to resolve our remaining differences," he declared. House Speaker Newt Gingrich (R-Ga.) responded the next day by offering to accept a "downpayment" of $80 billion in spending cuts over seven years. But such an agreement would still leave the two sides far apart and the government in limbo.

ON HOLD. If the stalemate continues, entitlement programs such as Medicare, Medicaid, and Social Security would grow unabated. It would be business as usual for welfare. But Republicans would use the impasse to hold down spending for most other domestic programs, including environmental protection, job training, and export promotion. Under the GOP's short-term spending strategy, programs funded by annual appropriations could be cut by as much as 25%. Overall, they would lose about $7 billion of the $248 billion they received last year.

The tax cuts that President Clinton and congressional Republicans promised are also on hold. And a fistful of credits that have expired during the past year are stuck in limbo. Among the victims: tax breaks for business research and employer-paid education expenses.

Atop all this sits the threat of default. On Jan. 22, Treasury Secretary Robert E. Rubin warned that by the end of February, Treasury will run out of funds to pay interest on bonds unless Congress raises the debt ceiling. Hard-line GOP lawmakers, such as House Majority Leader Richard K. Armey (R-Tex.), say they won't even address the matter for now, though a default would mean a huge rise in debt costs for businesses and individuals.

The endless stalemate is draining public confidence in government. "It touches on the national psyche," says Ford Motor Chairman Alexander J. Trotman. "The American public [is] somewhere between anxiety and annoyance." Given voters' malaise, Clinton and the GOP would be playing a dangerous game if they let the impasse continue through the fall elections.

The President would try to convince voters that he can save them from radical Republicans. But Democratic consultant Brian Lunde warns: "He can't be seen as protector of the old order. The Republicans will paint him as a tax-and-spend Democrat." The GOP is at risk as well. In many polls, 70% of Americans blame the party for the budget impasse. And in a Harris survey of 1,055 adults polled on Jan. 18-22, some 52% say they are inclined to back the President when the two sides disagree. That will make it tough for Republicans to sell a positive message should their pledge to balance the budget and cut taxes come to naught. "This is the equivalent of two guys playing Russian roulette," says a GOP consultant. "And there may be enough bullets for both of them."

Voter fury will only increase as the consequences of the bickering are felt. Part of government—including the Pentagon, Congress, and the White House—is funded through September, as are many high-profile programs,

SOFTER WORDS, BUT...

Clinton talked compromise in his speech, and Gingrich later sounded more flexible. But the dangerous game drags on

THE FALLOUT *Consequences of a continuing budget crisis*

ENTITLEMENT BALLOON Outlays for Medicare, Medicaid, Social Security, welfare, and other mandatory programs will grow unchecked, to more than $900 billion in fiscal 1997—7% higher than in fiscal 1995.

GOP SQUEEZE Spending for environmental protection, education, federal research, and the like would fall slightly this year from the 1995 level of $248 billion as congressional Republicans squeeze funding.

TAX LIMBO Business tax credits for R&D and employer-paid education expenses and levies such as the airline ticket tax have expired for the duration. All told, the feds are losing $100 million a week in tax revenues.

from national park visitor services to criminal law enforcement. But most operations will suffer a series of temporary spending bills, making long-term planning impossible.

The Environmental Protection Agency expects to make only about half its usual number of inspections. And business-backed deregulation is stalled, since money for technical analysis of new, more lenient rules has dried up. At the Justice Dept., criminal prosecutions would continue normally, but new civil cases may be on indefinite hold.

The Commerce Dept., a top target of GOP budget-cutters, already has nearly 1,600 export licenses worth $3 billion in its pipeline because of the last government shutdown. It could be May before the backlog gets cleared. And a 25% spending cut would only make matters worse. "We're creating a mind-set abroad that America is unreliable," says William A. Reinsch, Under Secretary for Export Administration. Squeezed between budget cuts and growing demand for visas and passports, the State Dept. is trimming its trade work, too.

After two federal shutdowns, the Occupational Safety & Health Administration faces a backlog of 1,000 complaints. A 25% funding cut would leave the agency unable to do routine inspections. Another Labor Dept. project in jeopardy: a summer jobs program for 600,000 kids. With funding uncertain, local governments will find it tough to recruit businesses to provide the jobs.

IN DOUBT. Ripple effects will hit state and local governments. States get $225 billion—more than 30% of their funding—from Washington. Most of it comes from Medicaid and welfare, both funded for now, but in doubt for the future. An additional $75 billion comes from targeted grants—many of which would be trimmed under the 25% spending cut. Worse, most states have only a month or two to wrap up their legislative budget sessions, and they can't plan. In Colorado, 40% of air and water quality programs are funded by Washington. "It throws everything into a cocked hat," says state Budget Director George Delaney.

If the standoff continues? Clinton can block the GOP from reforming entitlements. Republicans can stop the President from spending as much as he would like on other domestic programs. But nobody can make a policy decision on what the government should be doing and how it should be paying for it.

By Howard Gleckman, with Paul Magnusson and Susan B. Garland, in Washington

ALL HAIL GREENSPAN!

How the Fed boss has amassed power on the eve of a third term

From his introverted personality to his solicitous treatment of colleagues, Federal Reserve Chairman Alan Greenspan doesn't fit the image of a dictator. He lacks the intimidating presence of his 6-foot-7 predecessor, Paul A. Volcker, and eschews the professorial arrogance of 1970s Fed boss Arthur F. Burns.

Yet Greenspan has emerged as one of the most powerful chairmen in the 82-year history of the nation's central bank. His deft maneuvering within the Fed has minimized strong challenges to his monetary decisions. His solid stewardship of the economy has won raves from Wall Street. And his good political fortune—the GOP's capture of Congress—has all but guaranteed that President Clinton will renominate him for a rare third term on Mar. 2. "He is extremely powerful," concedes an Administration official. "During a third term there will be no discipline. He won't have to kowtow to anyone."

Already, dissent has all but vanished at meetings of the 12-member Federal Open Market Committee, which sets short-term interest rates. Formal votes of opposition, which averaged 10 a year during his first term (1987-1991), fell to five in 1994 and just two in 1995. Instead, says a colleague, Greenspan "walks into every FOMC meeting with eight or nine votes in his pocket." By contrast, Volcker faced an insurrection during his second term, with a majority of members forcing him to accede to their demand for a discount-rate cut.

"ENLIGHTENED DESPOT." Greenspan has so successfully forged consensus in part because strong-willed voices at the central bank have largely disappeared. Longtime Fed watchers say the current crop of 12 regional bank presidents is less steeped in economics and monetary policy than their predecessors. Having come up through the check-clearing ranks, the presidents are intimidated by Greenspan's knowledge and experience. "There are very few global thinkers among the presidents," says one Fed official.

Indeed, the 69-year-old Fed chief seems so confident that he won't be challenged that he has stopped calling some regional bank presidents before key FOMC meetings to determine their views. The presidents don't seem bothered by the change, since Greenspan is careful to solicit their opinions at meetings. Moreover, he has won their support by agreeing to set interest rates during FOMC meetings rather than exercising his prerogative to act between sessions—as has been a past practice. "Over time, everyone has become more confident in the job he has done," says longtime Philadelphia Fed President Edward C. Boehne.

Greenspan has few sharp rivals on the Fed's seven-member board of governors as well. A vocal critic on the right, inflation hawk Wayne D. Angell,

left the board in 1994. And Greenspan's most powerful challenger on the left, Vice-Chairman Alan S. Blinder, in February will return to Princeton University. Board differences are also discouraged by a staff that has grown in influence. Fed governors grumble that they can't gain access to critical staff research going directly to Greenspan and complain that he and his staffers consulted with them on the 1995 Mexican rescue plan only at the last minute. Moreover, he holds total sway over bank regulatory issues. Still, the governors shrug off the slights: "He may be a despot, but he's an enlightened despot," jokes one senior Fed official.

If Clinton had free rein, say White House aides, he would dump Greenspan in favor of a Fed chief concerned less with cutting inflation and more with economic growth. But with Senate Republicans insisting on Greenspan's reappointment, Clinton is considering a strong counterbalancing personality for vice-chairman: Wall Street financier Felix G. Rohatyn, a liberal Democrat and pro-growth champion. But Rohatyn may not make it past hostile GOP senators. Even if Greenspan and a pro-growth candidate were presented as a package, "I'd have real trouble signing off on a deal like that," says Senator Connie Mack (R-Fla.), chair of the Joint Economic Committee.

And so Greenspan's firm grip could remain unchallenged. Certainly, much of that power ultimately derives from the placid state of the economy: Should his quest to virtually eliminate inflation trigger a recession, Greenspan surely will find renewed challenges to his authority. Until that happens, though, the Fed's "enlightened despot" can call virtually any shot he likes.

By Dean Foust in Washington

TECHNOLOGY

WILL A NEW FILM CLICK?

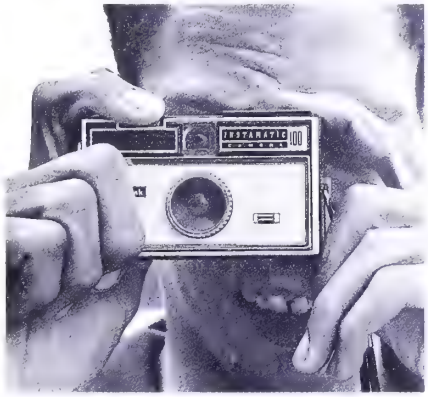
Kodak, Fuji, and other photo giants are betting that it will

The Instamatic. The 110. The Disc Camera. Every decade or so since the early 1960s, the photography industry has introduced a new film format designed to make cameras more portable and picture-taking simpler. And each time, after an initial flurry of enthusiasm, the snapshot-shooting public has returned to the higher quality of 35mm photography. In the absence of true innovation, conventional photo sales have slowed to a decidedly geriatric pace.

On Feb. 1, a consortium of five powerful companies will try once more, unveiling a new film and camera system that many believe could finally inject some life into the picture business. The Advanced Photo System (APS), which hits stores on Apr. 22, promises to combine the drop-in convenience of the Instamatic with near-35mm quality, while adding a host of new features.

"STREET SAMURAI." APS was dreamed up in the late 1980s by Eastman Kodak Co. executives worried by tepid industry growth trends. Recognizing that a new format would need industrywide backing, Kodak recruited camera makers Canon, Minolta, and Nikon—even arch-rival Fuji Photo Film Co.—to cooperate on research and development. "It was a real challenge to get our people to view Fuji as an ally while simultaneously viewing them as a samurai on the street," recalls Peter M. Palermo Jr., a now retired Kodak executive who piloted the project in its early years.

Mutual tolerance appears to have paid off. Among the consortium's technical advances is a new, far thinner polyethylene napthalate backing, the plastic to which silver-halide emulsion is applied. That, and an image size 43% smaller than 35mm, makes APS cartridges much more compact, cutting camera size by 10% to 30%. Also, the APS cartridge has no leader; just drop it in and it automatically winds, virtually eliminating loading problems.



FLASHY NEW FEATURES: The Instamatic offered drop-in convenience, but APS has a magnetic strip that allows "smart" photofinishing gear to fix mistakes

At the heart of the new system is a magnetic coating that enables the film, camera, and photofinishing equipment to communicate. As the camera shutter fires, information about lighting conditions, f-stop, and shutter speed are recorded on magnetic strips at the frame's edge. A new generation of smart photofinishing gear reads that data, automatically adjusting an underexposed frame, for example.

To simplify reprints, each developed APS roll will come with an index print, a sheet with thumbnail-size pictures of each frame. Consumers won't see negatives at all: The film will be rewound in its original cartridge. "The system is remarkably consumer-friendly," says Wayne Freedman, vice-president of marketing at Wolf Photo Inc., an Atlanta-based chain. "It's the biggest thing to happen in our business since the one-hour minilab. The unanswered question is: How will consumers respond?"

LASTING GROWTH? Indeed. No one doubts that APS will prove a hit. "Over time, we expect this will become the primary format in the market," says William J. Janawitz, Kodak's general manager in charge of the project. Kodak research suggests that 9 out of 10 consumers would like to have APS-like features if they were going to buy a new camera—even though the new products initially are likely to cost at least 10% to 20% more.

But will the system ignite lasting growth? "It will displace 35mm eventually, but I don't think it will change people's consumption pattern," says Prudential Securities analyst B. Alex Henderson. Privately, some Kodak executives share Henderson's fear that APS could primarily cannibalize 35mm sales. If so, the industry will have lost on an enormous bet. Kodak alone has committed $300 million to build new APS manufacturing capacity, after spending hundreds of millions on research.

Even if overall demand fails to increase, though, the new technology likely will knock out some marginal competitors that have flourished by producing private-label film and inexpensive Asian-made cameras. The big players who have invested in R&D will have a true edge for the first time in years—and their profit margins should fatten accordingly. That's more than Kodak could ever say of its Disc Camera.

By Mark Maremont in Boston

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INVESTIGATIONS

IS SOMEONE SNEAKING A PEEK AT *BUSINESS WEEK*?

Early trading of a few *Inside Wall Street* stocks raises a red flag

On most Thursday mornings, Seymour Zucker, the senior editor who oversees BUSINESS WEEK's *Inside Wall Street* column, sits down at a Bloomberg terminal and watches the market. On Thursday, Jan. 18, his attention was caught by Creative Biomolecules, a tiny biotech company that was favorably discussed in that week's column. All morning, the stock had hovered around 9. Then, at about 1 p.m., it began climbing—to 10—on heavy volume. "It really hit me between the eyes," recalls Zucker. In all, some 692,000 shares were traded, vs. an average volume of 245,500 during the previous five days.

Inside Wall Street, written by Gene Marcial, often causes stocks to move. But the action usually takes place on Friday. BUSINESS WEEK, which goes to press on Wednesday evening, is not available to the public until 5:15 p.m. Thursday—after the markets close. Zucker worried that the Thursday move meant someone may have gained premature access to the column and was trading on nonpublic information.

Creative Biomolecules was only the latest example in a pattern of suspicious Thursday trading that had begun several months earlier—and eventually involved some 11 stocks. Seven instances seemed especially graphic (table). The other four: Palomar Medical Technology, Pier 1 Imports, Kellstrom Industries, and Rentrak.

POWWOW. On Jan. 19, Zucker, Editor-in-Chief Stephen B. Shepard, and Kenneth M. Vittor, general counsel for The McGraw-Hill Companies, publisher of BUSINESS WEEK, met to discuss the issue. While the evidence was circumstantial, they agreed that signs of wrongdoing had become compelling enough to warrant alerting regulatory authorities. Vittor informed officials at the Securities & Exchange Commission, New York Stock Exchange, American Stock Exchange, and NASDAQ Stock Market. Now, McGraw-Hill is cooperating with the surveillance officials, who all declined to comment for this story.

A big Thursday jump in volume and price by *Inside Wall Street* stocks happens occasionally. But Zucker is almost always able to attribute the movement to such factors as earnings announcements, news events, or brokerage recommendations. At other times, inexplicable activity can simply be the result of the vagaries of the market.

In recent years, BUSINESS WEEK has strengthened its safeguards against possible leaks. The reason: Beginning in 1988, the magazine suffered a series of breaches in its security system. Some 11 individuals, including three stockbrokers, were convicted of—or settled—charges related to insider trading on information from *Inside Wall Street*.

Some of the people involved had obtained early copies of the magazine from printing plants in Old Saybrook, Conn., and Torrance, Calif., owned by R.R. Donnelley & Sons Co. They, in turn, passed tips on to others. Another person gained advance information through his employment at Applied Graphics Technology in Carlstadt, N.J., an outside production house for the magazine. Most disquieting to BUSINESS WEEK was the involvement of S.G. Ruderman, BUSINESS WEEK's radio broadcaster, who pleaded guilty to trading on inside information and went to prison.

"A RIGHT TO KNOW." Now, at the magazine's Manhattan headquarters, access to early copies is tightly restricted to a handful of people. Similar protections are used by America Online, which publishes an electronic version of the magazine around 7 p.m. on Thursday. Other restrictions are imposed on BUSINESS WEEK's four printing plants and far-flung distribution system, which ships more than 1 million copies weekly to subscribers and newsstands. "One hundred percent security doesn't exist," says Thomas Tully, McGraw-Hill's general manager of postal affairs and compliance. "If someone really wants to break the law, they can, but we've really tightened things up." Indeed, during the seven years since the 1988 breaches, BUSINESS WEEK has not detected any other consistent pattern of suspicious trading.

After alerting regulators, BUSINESS WEEK decided to disclose the suspicious trading here and in a news release. "Our readers have a right to know," says Editor-in-Chief Shepard. "And we are determined to protect the integrity of the magazine."

By Chris Welles in New York

AROUSING SUSPICIONS *Some of the stocks in which BUSINESS WEEK has noted unusual trading patterns.*

STOCK	ISSUE DATE	WED. DEADLINE*	WED. STOCK PRICE**	THURS. STOCK PRICE**	TRADING VOLUME	AVG. VOLUME 5 PREV. DAYS
STRATASYS	9/11/95	8/30/95	15 3/8	16 1/2	278,700	21,000
RESEARCH FRONTIERS	9/25/95	9/13/95	14	15 1/8	316,300	94,700
IVAX	10/2/95	9/20/95	29	31	1,363,500	537,400
SALTON/MAXIM	10/16/95	10/4/95	2 1/2	3	151,600	44,800
VTEL	11/27/95	11/15/95	21 3/4	22 5/8	773,800	566,400
LUMEX	1/15/96	1/3/96	9 1/8	10 3/4	72,500	9,700
CREATIVE BIOMOLECULES	1/29/96	1/17/96	8 3/8	9 1/8	692,000	245,500

*Date BUSINESS WEEK goes to press **Closing price

DATA: BLOOMBERG FINANCIAL MARKETS, BUSINESS WEEK

The SEC and the exchanges have been alerted to possible insider trading spotted by a senior editor

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CORPORATE PROFITS

WHO RAINED ON THE PARADE?

After a sunny year, fourth-quarter earnings look a little soggy

The big profit balloon looks to be losing air. Corporate earnings actually **dropped 2%**, on an **8% sales gain**, in BUSINESS WEEK's flash report on 83 companies' fourth quarter. This after just **11% growth** in the third quarter. The blame rests largely with a few big accounting charges: **McDonnell Douglas** took a **$1.8** billion hit, and **Amoco**, **Chevron**, and **Texaco** wrote off a combined **$1.7** billion in impaired assets. Exclude those, and overall profits were **up 13%**. The winners: High-tech giants, led by **IBM**'s **39%** profit gain, and **Intel**'s **133%** surge. —*Fred Jespersen*

	CURRENT QTR. SALES (MILLIONS)	% CH
INDUSTRIALS	201,642.4	+9
ALCOA	3,107.8	+18
AMERICAN BRANDS	3,084.6	–18
AMOCO	6,972.0	+2
ARMSTRONG WORLD INDUSTRIES	497.7	–2
BAUSCH & LOMB	455.1	–6
BOISE CASCADE	1,242.0	+12
BRISTOL-MYERS SQUIBB	3,608.0	+11
CATERPILLAR	4,213.0	+7
CHAMPION INTERNATIONAL	1,740.9	+19
CHEVRON	9,157.0	–1
CHRYSLER	15,057.0	+6
CONAGRA	6,626.3	+5
CORNING	1,338.7	+5
DUPONT	10,679.0	+3
EASTMAN KODAK	4,092.0	+6
EXXON	30,666.0	–1
GENERAL ELECTRIC	19,752.0	+11
GEORGIA-PACIFIC	3,410.0	+2
GILLETTE	1,987.9	+10
IBP	3,160.3	–2
INLAND STEEL INDUSTRIES	1,121.7	–3
INTERNATIONAL PAPER	5,100.0	+24
JOHNSON & JOHNSON	4,846.0	+18
LOCKHEED MARTIN	6,052.0	–8
McDONNELL DOUGLAS	3,731.0	+6
MERCK	4,556.9	+18
MOBIL	19,766.0	+3
MONSANTO	2,114.0	+7
PFIZER	2,744.3	+24
PPG INDUSTRIES	1,722.4	+4
REYNOLDS METALS	1,872.0	+11
ROCKWELL INTERNATIONAL†	3,062.0	+25
TEXACO	9,652.0	+8
UNION CARBIDE	1,399.0	+7
WEYERHAEUSER	3,055.8	+12
SERVICES	42,392.7	+1
AMERICAN EXPRESS	4,048.0	+6
AMR	4,188.0	+9
BANKAMERICA	NA	NA
BANKERS TRUST NEW YORK	NA	NA
CHASE MANHATTAN	NA	NA
CHEMICAL BANKING	NA	NA
CITICORP	NA	NA
COMPUSA	931.2	+21

CORPORATE PROFITS

CTRL-ALT-SLOWDOWN

PC makers are facing less-than-expected sales growth

Time for personal computer companies to think about pushing the reboot button. After phenomenal growth of more than 20% in each of the past two years, PC sales are finally slowing. And it's happening all too quickly for some PC makers and retailers.

That's evident from the earnings hit many companies are taking. Apple Computer Inc. and AST Research reported fourth-quarter losses, and Intel, Dell Computer, and retailer Best Buy each have announced weaker-than-expected profits in recent weeks. On Jan. 19, Packard Bell Electronics Inc. handed out pink slips to 250 workers after it lowered its outlook for the first half of 1996. IBM says it posted double-digit sales increases in PCs, but analysts think it barely eked out a profit in the segment.

Even high-flying Compaq Computer Corp. is turning wary. On Jan. 24, it reported strong fourth-quarter earnings, excluding special charges, of $323 million, up 33% from the same period last year, on revenues that were up 45% to $4.7 billion. But Compaq's share price fell 1¾ points, to 47¾, when CEO Eckard Pfeiffer warned that price-cutting would continue to cut into gross margins this year. "We are moving forward with a clear goal of continued market share growth. That requires timely pricing actions," says Pfeiffer.

The troubles are more than a momentary blip on the screen. Sanford C. Bernstein & Co. is projecting that U.S. PC sales growth will fall to just 15.2% this year and will keep falling in the following two years. The sizable decline

ITS NS)	% CHG.	EST. EPS (11/14)	REPORTED EPS	DIFF.
7	**–22**	1.07	0.92	–0.15
9	**–59**	1.22	0.85	–0.37
1	**–67**	0.90	0.85	–0.05
0	**–61**	1.15	0.42	–0.73
6	**NM**	1.13	–2.09	–3.22
4	**NM**	0.81	–0.04	–0.85
4	**+172**	1.51	1.15	–0.36
0	**NM**	1.26	1.28 *	+0.02
0	**+8**	1.23	1.53	+0.30
5	**+113**	2.41	2.26	–0.15
0	**NM**	0.77	–0.64	–1.41
0	**–11**	2.27	2.67	+0.40
1	**+11**	0.72	0.72	—
5	**+139**	0.38	0.37	–0.01
0	**–3**	1.21	1.13	–0.08
0	**NM**	0.94	0.80	–0.14
0	**–12**	1.24	1.35	+0.11
0	**+11**	1.11	1.12	+0.01
0	**+17**	3.23	2.17	–1.06
1	**+16**	0.52	0.52	—
0	**–27**	0.76	0.59	–0.17
9	**–31**	0.50	0.47	–0.03
0	**+71**	1.28	1.01	–0.27
0	**+23**	0.68	0.72	+0.04
7	**+15**	1.35	1.56	+0.21
0	**NM**	1.67	1.68 *	+0.01
8	**+11**	0.70	0.70	—
0	**+48**	1.70	1.93	+0.23
0	**+48**	0.73	0.65	–0.08
.6	**+24**	0.65	0.64	–0.01
.2	**+7**	0.89	0.83	–0.06
.0	**+22**	1.54	1.15	–0.39
.0	**+25**	0.85	0.88	+0.03
.0	**NM**	1.05	–1.02	–2.07
.0	**+21**	1.08	1.21	+0.13
.9	**+33**	1.39	1.25	–0.14
.8	**+32**	1.26	1.42	+0.16
.0	**+15**	0.77	0.77	—
.0	**NM**	0.97	1.15 *	+0.18
.0	**+19**	1.65	1.74	+0.09
.0	**+25**	1.47	1.36	–0.11
.0	**+48**	1.42	1.70	+0.28
.0	**+174**	1.62	1.81	+0.19
.0	**–13**	1.66	1.72	+0.06
.4	**+80**	0.57	0.80	+0.23

	CURRENT QTR. SALES (MILLIONS)	% CHG.	QTR. PROFITS (MILLIONS)	% CHG.	EST. EPS (11/14)	REPORTED EPS	DIFF.
CSX	2,771.0	+9	276.0	**+15**	1.04	1.31	+0.27
DISNEY (WALT)†	3,818.0	+16	496.0	**+3**	0.51	0.93	+0.42
FEDERAL EXPRESS††	2,547.0	+8	89.9	**+4**	1.70	1.57	–0.13
FIRST INTERSTATE BANCORP	NA	NA	215.4	**+2**	2.87	2.66	–0.21
HILTON HOTELS	457.6	+12	63.1	**+66**	0.95	1.30	+0.35
MERRILL LYNCH	5,293.0	+18	303.0	**+87**	1.42	1.49	+0.07
MORGAN (J.P.)	2,609.0	+10	366.0	**+90**	1.64	1.80	+0.16
NATIONSBANK	NA	NA	510.0	**+26**	1.91	1.85	–0.06
NORTHWEST AIRLINES	2,201.5	+9	3.6	**–90**	0.75	–0.10	–0.85
PAINEWEBBER GROUP	1,374.4	+32	58.8	**NM**	0.49	0.50	+0.01
SCHWAB (CHARLES)	394.8	+46	42.6	**+26**	0.26	0.24	–0.02
TRAVELERS GROUP	4,263.7	–3	441.7	**+32**	1.25	1.32	+0.07
UAL	3,667.0	+7	–18.0	**NM**	2.93	–4.15	–7.08
UNION PACIFIC	1,974.0	+19	179.0	**+21**	1.21	0.87	–0.34
USAIR GROUP	1,854.5	+10	60.3	**NM**	0.00	0.61	+0.61
WELLS FARGO	NA	NA	306.0	**+42**	5.61	6.29	+0.68
TECHNOLOGY	62,859.4	+17	4,969.6	**+30**	1.34	1.29	–0.05
ADVANCED MICRO DEVICES	593.0	+9	55.6	**+36**	0.56	0.52	–0.04
APPLE COMPUTER†	3,148.0	+11	–69.0	**NM**	0.80	–0.56	–1.36
COMPAQ COMPUTER	4,701.0	+45	82.0	**–66**	1.18	1.17 *	–0.01
CONNER PERIPHERALS	776.7	+31	25.3	**–43**	0.35	0.40	+0.05
DIGITAL EQUIPMENT††	3,951.4	+14	148.8	**+688**	0.87	0.91	+0.04
GENENTECH	221.9	+7	25.6	**+38**	0.33	0.21	–0.12
IBM	21,920.0	+10	1,711.0	**+39**	3.48	3.66 *	+0.18
INTEL	4,580.0	+42	867.0	**+133**	1.11	0.98	–0.13
MICROSOFT††	2,195.0	+48	575.0	**+54**	0.84	0.90	+0.06
MOTOROLA	7,298.0	+13	432.0	**–16**	0.93	0.72	–0.21
RAYTHEON	3,360.0	+23	222.3	**+8**	0.91	0.92	+0.01
SUN MICROSYSTEMS††	1,751.4	+19	126.0	**+54**	0.58	0.65	+0.07
TEXAS INSTRUMENTS	3,603.0	+30	291.0	**+55**	1.58	1.50	–0.08
XEROX	4,760.0	+4	477.0	**+53**	3.22	3.91	+0.69
UTILITIES & TELECOM	27,371.0	+3	2,314.6	**–13**	0.64	0.62	–0.02
AMERICAN ELECTRIC POWER	1,425.0	+11	131.4	**+27**	0.65	0.70	+0.05
AMERITECH	3,531.8	+11	412.7	**–4**	0.87	0.74	–0.13
BELL ATLANTIC	3,154.2	–10	395.4	**+26**	0.89	0.90	+0.01
BELLSOUTH	4,765.0	+8	–99.0	**NM**	0.56	0.57 *	+0.01
GENERAL PUBLIC UTILITIES	931.0	+10	80.8	**+27**	0.51	0.59	+0.08
NYNEX	3,304.3	–3	235.6	**+19**	0.86	0.55	–0.31
PACIFIC GAS & ELECTRIC	2,227.2	–15	227.1	**+119**	0.53	0.48	–0.05
PACIFIC TELESIS GROUP	2,282.0	–3	231.0	**–12**	0.55	0.54	–0.01
SBC COMMUNICATIONS	3,442.5	+7	517.8	**+22**	0.83	0.85	+0.02
SOUTHERN	2,308.0	+21	181.8	**–8**	0.26	0.24	–0.02

† First-quarter results †† Second-quarter results NM = not meaningful NA = not available *EPS adjusted for special items

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE McGRAW-HILL COMPANIES. EARNINGS ESTIMATE DATA PROVIDED BY I/B/E/S INTERNATIONAL INC., NEW YORK, NY. I/B/E/S IS A REGISTERED TRADEMARK OF I/B/E/S INTERNATIONAL INC

is already hitting some component makers. At Intel Corp., higher marketing costs drove up fourth-quarter selling and administrative expenses by 42%, to $569 million, during the quarter. Quarterly earnings more than doubled anyway, to $867 million on sales of $4.6 billion, but even that was below Wall Street's expectations.

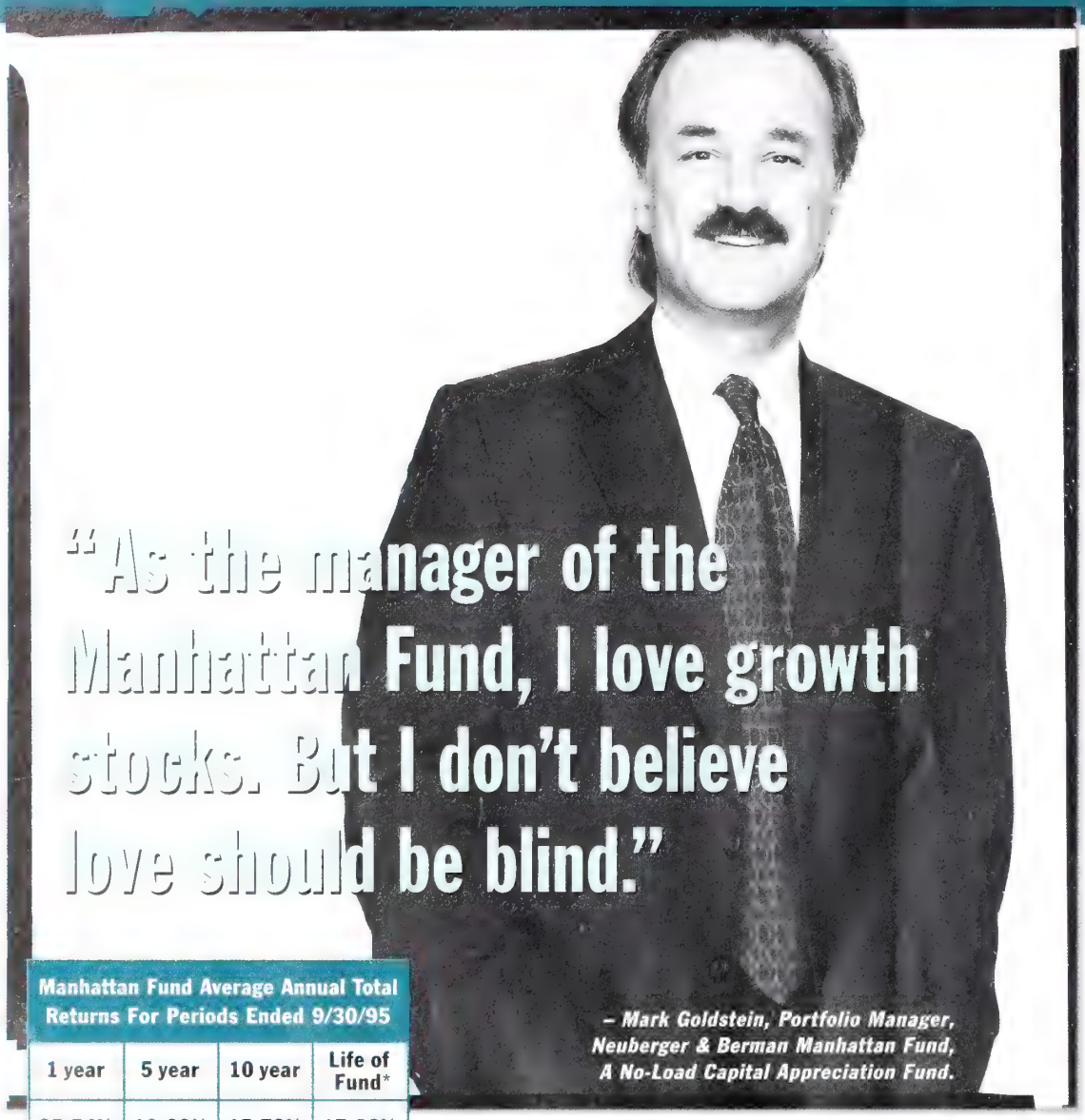
BRIGHT SPOT. There is a plus side. With Internet use expanding like mad, International Data Corp. predicts that sales of servers, which manage networks of PCs, will jump 38%, to $3 billion in 1996. IDC also figures U.S. notebook PC sales will grow 23% this year, to $12.2 billion, up from a 12.6% rise in 1995.

STICKER SHOCK: *Last year, average consumer PC prices rose 8%*

Microsoft is another bright spot. In the latest quarter, its earnings soared 54%, to $575 million, on strong sales of its Windows 95 software.

But some outsiders think the surge of Win95 upgrades this year will be less than expected, partly because many companies are holding off on the costly conversion. PC sticker shock is another worry. Last year, average consumer PC prices rose 8%, twice the historical rate, to $1,875, figures market researcher IDC/Link Inc. You can just about hear PC executives mumbling: "Now, which key do we hit to make them keep buying?"

By Gary McWilliams in Houston, with bureau reports



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– Mark Goldstein, Portfolio Manager, Neuberger & Berman Manhattan Fund, A No-Load Capital Appreciation Fund.

Manhattan Fund Average Annual Total Returns For Periods Ended 9/30/95

1 year	5 year	10 year	Life of Fund*
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*Neuberger & Berman Management Inc. became investment adviser to the predecessor of this Fund on 3/1/79. Performance before the Fund's August 1993 reorganization is for its predecessor. Investment returns and principal fluctuate. Past performance is no guarantee of future results. Redemption proceeds may be higher or lower than original cost. ©1996 Neuberger & Berman Management Inc., Distributor.

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EDITED BY KEITH H. HAMMONDS

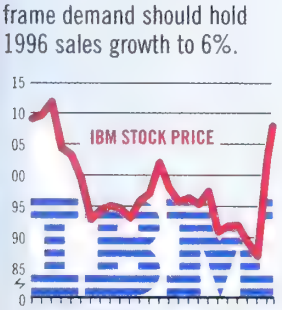
NO WEDDING MARCH OF THE TOYS

CAN BARBIE AND G.I. JOE FIND happiness together? Not likely. Hasbro, Joe's parent, rejected a surprise $5.2 billion acquisition offer on Jan. 24 from archrival Mattel, maker of Barbie and Cabbage Patch Kids. The companies had been discussing a merger since April. But Hasbro's board argued that merging the world's two biggest toymakers, whose combined sales of $6 billion represent a quarter or more of the industry, would raise antitrust issues. That doesn't worry smaller rivals: "I can't say we'd be delighted, but I don't think we'd oppose it," says Tyco Toys Chairman Richard Grey. More likely, Hasbro just doesn't want to play. Ultimately, though, it may have little choice: After a string of strategic miscues, its shares have languished for three years.

CLOSING BELL

BIG BLUE MARVEL

IBM's hidden jewel is information technology services—operations that run data centers and computer help desks. The business exploded in 1995, its revenues soaring 31%, to $12.7 billion. Add revived PC sales and the acquisition of Lotus Development, and the fourth quarter sparkled. Net profits of $4.2 billion topped expectations, lifting IBM shares 18% in two days. Don't get too used to the fireworks, though: A slower economy and sated mainframe demand should hold 1996 sales growth to 6%.



DATA: BLOOMBERG FINANCIAL MARKETS

WELLS FARGO BAGS ITS PREY

AFTER CLINGING FOR THREE months to the specter of a merger with First Bank System, First Interstate Bancorp instead succumbed on Jan. 24 to Wells Fargo's hostile bid. The $11.6 billion price tag isn't any higher than Wells's earlier offer. But First Interstate's hand was forced by big investors such as Kohlberg Kravis Roberts, sources say, and by an unfavorable accounting ruling from the Securities & Exchange Commission. "They played a game of chicken and lost," says Donaldson, Lufkin & Jenrette Securities analyst Tom Brown. That said, the losers don't make out badly: First Interstate CEO William Siart will walk away with a $4.6 million paycheck. And First Bank gets $200 million for having its friendly deal broken up.

BANKERS TRUST BITES A BULLET

BANKERS TRUST PUT A DARK coda on its lackluster 1995 results, agreeing on Jan. 24 to terminate disputed derivative contracts for $67 million with Air Products & Chemicals. Bankers says its fourth-quarter results reflected the settlement and added that it was pleased to put a fight with "a valued client" behind it. Now, Wall Streeters are betting on when Bankers will settle its last remaining derivatives litigation, a nasty, high-profile dispute with Procter & Gamble. Bankers and P&G representatives met on Jan. 19 but failed to reach an agreement. A trial is set for May.

HEADLINER: MICHAEL ARMSTRONG

HUGHES STRIKES GOLD IN OUTER SPACE

Suddenly, Mike Armstrong is cruising Hollywood's fast lane. On Jan. 23, a day after snagging $137.5 million from AT&T for a 2.5% stake in his DirecTV unit, the Hughes Electronics CEO fielded congratulatory calls from Viacom CEO Sumner Redstone and other media honchos.

The deal brings AT&T's clout to a satellite-to-home broadcasting service already thriving: 1.3 million households pay about $30 a month for DirecTV's 175 channels. Within months, AT&T will market DirecTV to its long-distance phone customers. It also plans to sell Hughes's DirecPC, transmitting Internet multimedia data to home computers. "By the end of the year, we will have a whole complement of services in the market," says Armstrong.

Big talk? Armstrong has delivered before. After turning around IBM's European unit, he took over Hughes in 1992. He transformed the stagnant defense contractor, boosting margins and launching promising ventures—DirecTV among them. The result: Hughes shares have climbed to $53 from $15 since his arrival.

By Eric Schine

B&L REWRITES THE BOOKS

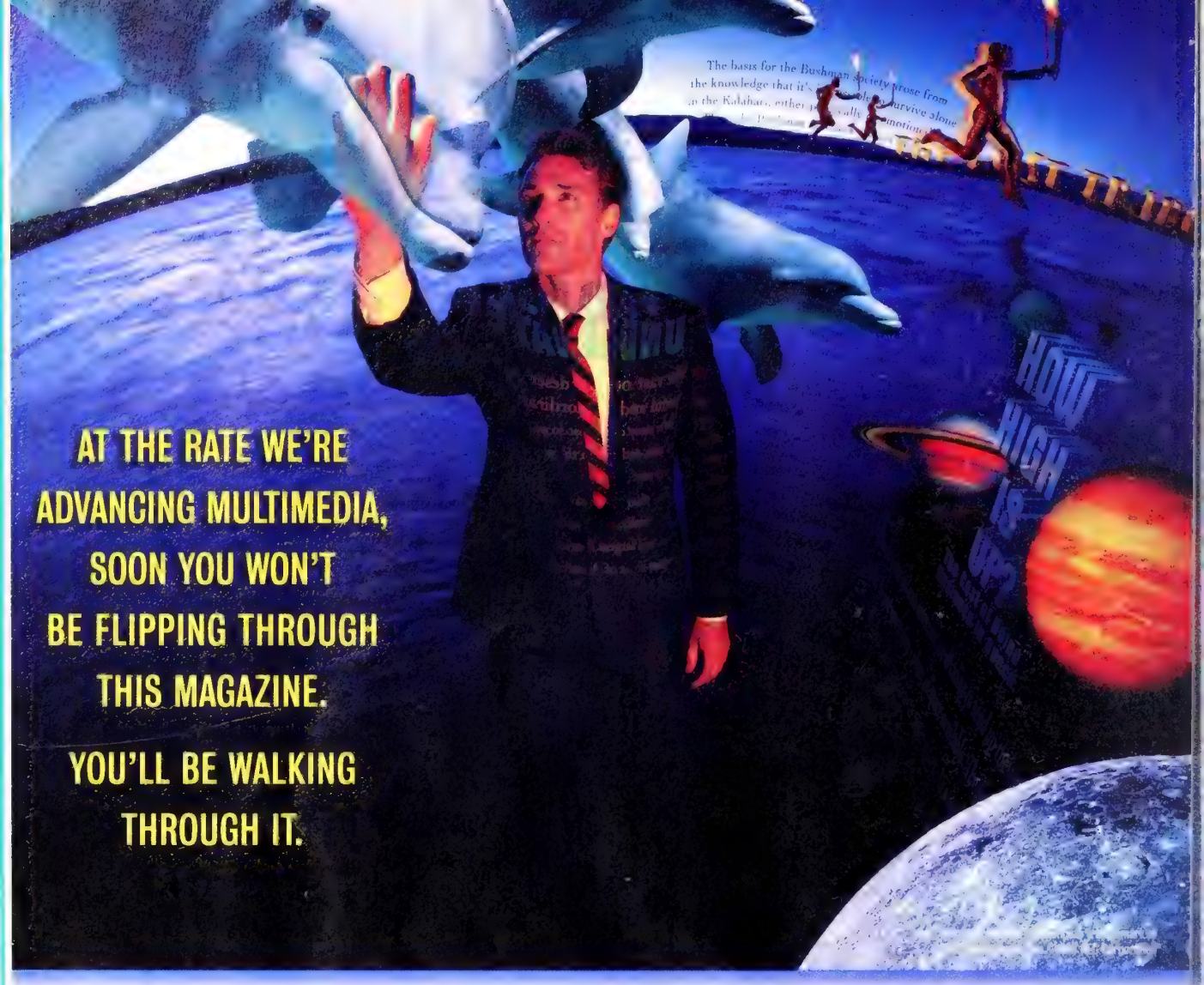
CONTINUING HIS EFFORTS TO clean up Bausch & Lomb, interim CEO William Waltrip on Jan. 24 restated the company's 1993 and 1994 earnings. The unusual move follows a BUSINESS WEEK story (Oct. 23) exposing accounting and ethical abuses. B&L is reversing $42.1 million of questionable 1993 sunglass and contact-lens sales, cutting net income for that year by $17.6 million. Its 1994 results increase by similar amounts. Waltrip calls the restatement voluntary and says B&L didn't materially breach accounting rules. But the action won't end an SEC investigation.

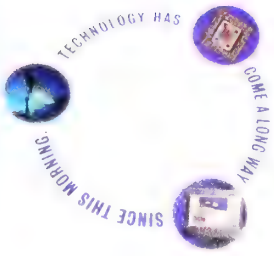
SO MUCH ANGER AT THE AARP

THE AMERICAN ASSOCIATION of Retired Persons has drawn fire from the GOP Congress for lobbying for big-ticket items such as Medicare and Social Security. Now many AARP members are ticked off, too. While the AARP officially claims its membership remains flat at about 33 million, insiders say the organization is alarmed by recent losses totaling 1 million members, many of whom were angered by its opposition to federal budget cuts. The AARP hopes to target older baby boomers, in part by revamping its magazine, *Modern Maturity*.

ET CETERA . . .

- The Food & Drug Administration finally approves Procter & Gamble's olestra.
- Premier Industrial agrees to sell out to Britain's Farnell Electronics for $2.8 billion.
- Spyglass will pay $9.5 million for Stonehand, a maker of Internet publishing software.
- Former Lotus Development Chief Jim Manzi resurfaces as CEO of Industry.Net.





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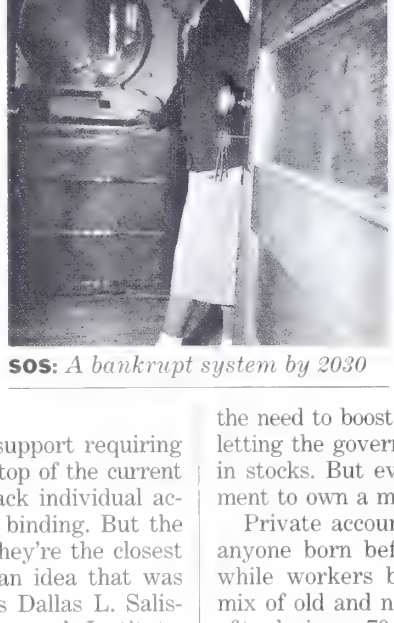
EDITED BY DOUGLAS HARBRECHT

PRIVATIZE SOCIAL SECURITY? NOBODY'S LAUGHING NOW

Conservatives long have dreamed about privatizing Social Security. They argue that the massive shortfalls projected in the 21st century for Uncle Sam's retirement system can be avoided only by giving back part of Social Security's annual $400 billion tax take to individuals to invest for retirement. But elected officials—afraid to touch politics' "third rail"—never paid much heed.

Until now. Social Security privatization is about to land on Washington's center stage—launched not by the GOP, but by a panel appointed by the Clinton Administration. The panel's explosive findings portend a battle that will make the fight over Medicare cuts look like a tea party.



SOS: *A bankrupt system by 2030*

In a report expected out by mid-February, five of the 13 members of the Advisory Council on Social Security will endorse replacing half of the retirement plan with Personal Security Accounts (PSAs). These accounts, funded by diverting 5% of wages from the 15.3% payroll tax, could be put in stocks, bonds, or other investments. Those funds are likely to pay a higher return than the benefits today's workers can expect from Social Security. The plan's goals: boost private savings and give Generation X workers proof that the system will exist when they follow baby boomers into retirement.

Two more panel members are likely to support requiring workers to set up small private accounts on top of the current system. So a majority of the group will back individual accounts. An advisory panel's findings aren't binding. But the recommendations will have clout, because they're the closest thing yet to an official endorsement for "an idea that was laughed out of town in the 1980s," marvels Dallas L. Salisbury, president of the Employee Benefit Research Institute.

STRONG LURE. No one's laughing now. At least three Washington think tanks are working on privatization studies. Securities, mutual-fund, and life-insurance interests are backing some of the research, drawn by the prospect of PSA balances that could hit $60 trillion by 2035. And while no action is likely until 1997, after the election, the idea is making waves in the campaign. GOP Presidential wannabe Malcolm S. Forbes Jr. has a privatization strategy, which front-runner Senator Bob Dole (R-Kan.) charges "would end Social Security as we know it." President Clinton is also unlikely to back the plan, though the Administration won't take a stand until the report is issued.

Why the ferment? Social Security will go broke during the baby boomers' retirement years. Although annual payroll taxes now exceed benefit payouts by $60 billion, the system's cash flow will turn negative sometime around 2014. By 2030, the cushion built by today's surpluses will disappear. Worse, those operating surpluses are now parked in Treasury bonds, which help mask the true federal budget deficit. By some calculations, the payroll tax on 21st century workers might have to nearly triple, to 40%, to fill the gap. "The one thing we all agree on is that the current system can't go on," says University of Michigan economist Edward M. Gramlich, chair of the advisory panel.

Another problem: Social Security no longer delivers the fat returns that past and current retirees have enjoyed. Today's 75-year-old single man can expect to get back all the taxes he and his employers paid with interest—plus a 75% windfall. For today's 65-year-old, the lifetime windfall shrinks to 25%. But for boomers, the oldest of whom are just turning 50, "anyone earning average or above-average wages won't even get back his or her taxes plus interest," notes benefit consultant Sylvester J. Schieber of Watson Wyatt Worldwide. Schieber helped draft the Advisory Council's PSA plan.

Even Social Security's old guard, led by the system's patriarch, ex-Social Security Commissioner Robert M. Ball, recognizes the need to boost returns. Ball and five other advisers advocate letting the government invest part of Social Security's surplus in stocks. But even Democrats quail at allowing the government to own a multitrillion-dollar stake in Corporate America.

Private accounts pose problems, too. Under the PSA plan, anyone born before 1943 would remain in the old system, while workers born between 1943 and 1968 would face a mix of old and new benefits. To pay for already earned benefits during a 70-year transition, Schieber proposes a new series of "Liberty Bonds" backed by an earmarked 1% national sales tax. At their peak, in 2050, the bonds could boost the national debt by $10.2 trillion, $1.2 trillion in '96 dollars.

Defenders of the system figure that huge price will kill privatization. They bet Congress will repeat the Social Security reforms of 1977 and 1983 by raising taxes and the retirement age and trimming benefits. "This system needs adjustment, but it's not fundamentally broken," says a White House aide.

Backers contend that tinkering isn't enough. "If you tell the American public: 'You can have a secure, funded pension and the cost is a 1% sales tax,' they're going to think that's a pretty good deal," says Schieber. Bargain or not, that deal will soon be on the table.

By Mike McNamee

The latest push for conversion of the present system is coming from a Clinton panel

GERMANY

REVOLUTION AT DAIMLER

Deutsche Bank is forcing an overhaul of the industrial giant. Will Germany Inc. ever be the same?

It was a very German coup—quiet, slow-motion, thorough. In a bare-bones press handout in June, 1994, Daimler Benz announced that Edzard Reuter would be replaced as chief executive by Jürgen E. Schrempp, head of Daimler Benz Aerospace (DASA) after the annual meeting the following May.

For Hilmar Kopper, chief executive of Deutsche Bank and chairman of Daimler's board of supervisors, Reuter's removal was the payoff for weeks of intense meetings with Daimler directors and advisers. Slowly, Germany Inc. woke up to what had happened: A powerful CEO had been overthrown by the company's bank and major shareholder.

NEW SCENARIO. Fast forward to January, 1996. Schrempp is now doing things Reuter would never contemplate. In mid-January, Schrempp folded the remnants of the money-losing AEG electronics subsidiary into other divisions. The cost: a write-off of $1.1 billion. Then came the real shocker. On Jan. 22, Schrempp cut off funding for Fokker Aircraft, the floundering Dutch airplane maker 51%-owned by Daimler. The probable fallout: Fokker's bankruptcy and a write-off for Daimler so huge it will report a 1995 loss of $4.2 billion.

What is happening at Daimler Benz is familiar enough in Corporate America these days. Major shareholder gets mad; shareholder boots out old CEO; new CEO gets tough. But in Germany, this scenario has until recently been a rarity. Boardroom politics are too consensual, and shareholders unaccustomed to rocking the boat. "There isn't even a phrase in German for 'shareholder activism' or 'corporate governance,'" says Hans Decker, former vice-chairman at Siemens who now teaches at Columbia University.

Yet Kopper is signaling that his bank, which holds 24% of Daimler, must be more active. "Deutsche Bank had to take a role in unseating Reuter," says Arie Y. Lewin, a professor at Duke University's J. B. Fuqua School of Business. "It's not the [German] stock market that's going to do it." If Kopper and Schrempp pursue their program to the end, the idea of shareholder-inspired restructuring could become part of the corporate mentality in Germany. Kopper even hints he might sell off a chunk of Deutsche Bank's $6 billion stake in Daimler—provided the price rises enough and punitive capital-gains taxes for large holding companies are legislated out of existence. Such a move would show other German investors that they too can profit by getting tough.

It's certain that both men want profound change. The focus for Daimler is now on cars, trucks, and those areas of aerospace that actually make money.

"It's profitability first and strategic fit second," says Schrempp. Meanwhile, Kopper has been anything but idle at Deutsche Bank. Deutsche, a lumbering giant, is facing global challenges. Its return on capital of 8% sadly lags the 20% of U.S. rival Citicorp. So he's pruning thousands of jobs in Germany and building a huge investment-banking business. Kopper acknowledges that Deutsche Bank has an image of being a financial battleship that is "extremely solid." Trouble is, he adds: "The age of battleships is over."

Another age may be ending in Germany—the era of patient capital where banks hold outright stakes in key companies for years. Deutsche, for example, has stock worth an estimated $15 billion in more than a dozen companies ranging from Daimler to insurer Allianz. Deutsche itself has been a Daimler partner since the 1920s, when it gained stock in a debt-for-equity swap. Deutsche cultivated a

FOKKER FALLOUT? *The company is in bankruptcy*

UTSCHE BANK AND DAIMLER BENZ: ERMANY INC.'s CORE PARTNERSHIP

COMPANIES Deutsche Bank is Germany's largest , with $400 billion in assets. Daimler Benz, with billion in sales, is Germany's biggest industrial pany, making everything from planes to autos.

PARTNERSHIP Deutsche Bank is Daimler's banker. More important, it holds 24% of Daim- equity, worth some $6 billion. Deutsche Bank f Hilmar Kopper chairs Daimler's supervisory board.

PROBLEM Deutsche Bank is getting an inade- e return on its Daimler shares and until recently little to promote badly needed change at the huge pany.

SOLUTION Kopper pushed out Daimler chief ard Reuter and cleaned out Daimler's management d. He installed Jürgen Schrempp, who is forcing a ful restructuring.

DATA: BUSINESS WEEK, COMPANY REPORTS

KOPPER AND SCHREMPP: *The two often consult face-to-face*

close relationship with its client, which used the bank's loans and capital-raising expertise to expand rapidly.

As executives, Schrempp and Kopper grew up inside this profoundly stable corporate world. Unlike most bank bosses these days, the 61-year-old Kopper worked his way up from banking apprentice. Kopper reached the bank's management board at 42 and assumed the top job after Alfred Herrhausen was assassinated by terrorists in 1989. Schrempp, 51, started at the bottom too, as an automotive apprentice at Daimler's luxury auto maker Mercedes-Benz, and had stints in the U.S. and South Africa before reaching the top.

While they were both climbing the corporate ladder, Kopper and Schrempp saw their world change dramatically. German manufacturers, forced to compete with global rivals and counter the effects of a rising Deutschemark, discovered they were often overstaffed and inefficient. German banks, facing international rivals too, needed every bit of capital for acquisitions and write-offs. The stock banks held in German companies began to look like poor investments.

It still took Deutsche a long time to wake up to the failure of Reuter's strategy. Even after he succeeded Herrhausen, Kopper did not immediately block any of Reuter's plans. "Kopper let Reuter do whatever he wanted," complains Ekkehard Wenger, finance professor at Würzburg University.

Some of Daimler's top managers were privately having doubts. When he needed backing for substantial layoffs at DASA in 1993, Schrempp, insiders say, opened back channels to both Kopper and Deputy Chairman Karl Feuerstein, the ranking official of labor union IG Metall at Daimler. When Kopper decided Reuter had to go, there was no doubt in his mind who would succeed him.

BIG BENZ: *Mercedes should post $2.4 billion in operating profits this year*

Yet critics point out that it was Schrempp who thought up the idea of buying 51% of Fokker in 1993. Complains one Frankfurt banker: "The manager responsible for dreadful mistakes is now in charge of the whole company." Schrempp now admits his blunder. Still, says Kopper, "Schrempp is the right man for the job." The market has certainly responded warmly to Schrempp's tough act. Since the announcement on Fokker, Daimler's German-traded shares have hit a 16-month high of $545. The U.S.-traded ADR shares are getting popular, too. San Diego's Brandes Investment Partners Inc., for instance, piled up 1.8 million U.S.-traded shares worth $94 million in six months. Says Brandes Senior Vice-President William A. Pickering: "[Schrempp] is finally taking steps to undo the diversification."

ESCAPE HATCH? Kopper must still figure out his designs for Deutsche's Daimler stake. A sell-off would realize billions—but also trigger a 60% capital-gains tax that holding companies have to pay. "No deal!" says Kopper. But he adds, "If Germany had a different pattern of tax and legislation, I would reorganize [our holdings]."

An escape hatch could spring open. The opposition Social Democrats may propose legislation whereby Deutsche and other banks could sell off industrial holdings without paying a huge capital-gains tax, provided that they reinvest the proceeds in the German economy. Kopper says he is open to discussion, but will fight any bill that dictates how he must invest. For now, Deutsche has no choice but to push for a turnaround at Daimler to unlock its value and achieve a better flow of dividends.

Failure to turn Daimler around would vindicate the pessimists who say Germany is too rigid to adapt to the global economy fast enough. But for Kopper and Schrempp, there can be no retreat. They have started a revolution—and revolutions have a way of continuing. Look for more upheaval at these two giant companies.

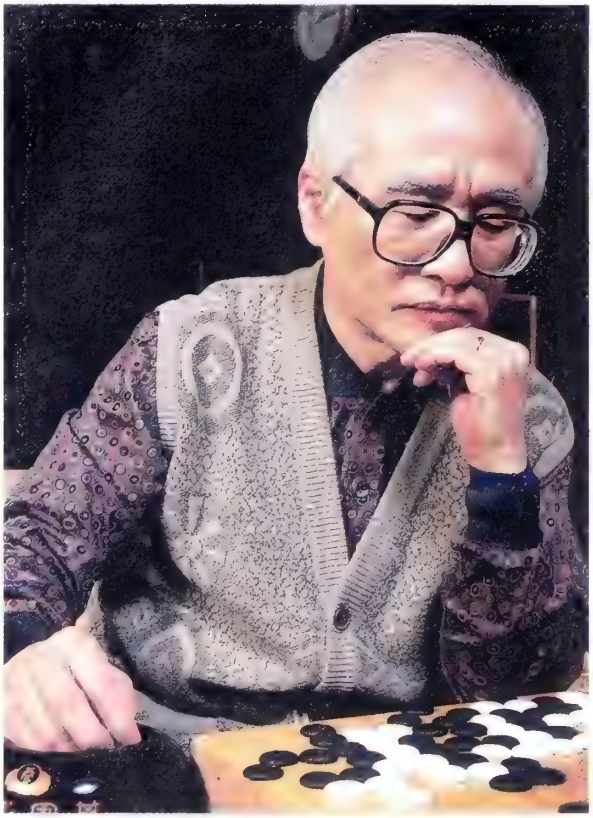
By John Templeman in Frankfurt and Stuttgart, with Christopher Power and William Glasgall in New York and bureau reports

SOUTH KOREA

EXILE OF THE PATRIARCH

Daewoo's founder is off to Vienna–but don't count him out

Armed with just $10,000, Kim Woo-Choong started the Daewoo group in the late 1960s by making cheap shirts for U.S. mass marketers. Partly thanks to his connections with South Korean governments, he was able to build Daewoo into a $57 billion industrial powerhouse, making autos, ships, electronics, and a wide array of other goods. The chain-smoking, silver-haired tycoon became a roving ambassador, circling the world in search of the next deal.



Now, the 59-year-old Kim is headed into exile. Officially, Daewoo says the boss's decision to base himself in Vienna is not connected with his current trial on two charges of paying bribes to former President Roh Tae Woo, who is at the center of a $650 million corruption scandal. In court, Kim has repeatedly said his payments to Roh were political contributions, not bribes. If Kim is convicted, he is expected to be fined or win a suspended sentence instead of facing jail time.

DARING PLAN. Despite company denials, the conclusion appears inescapable that Kim's plans to depart after his trial reflect his feeling that the investigation into past links between Korea's *chaebol* and its military-backed governments has been overtly political. Kim was not available for comment, but one source says going on trial is "sickening" to him.

As his replacement, Kim has appointed Yoon Young-Suk, previously chairman of Daewoo's heavy-industry unit, to run the whole group, with the exception of autos. Kim will now concentrate full-time on that business. "It is not really true that Chairman Kim is leaving Daewoo," says Yoon. "He wants a break to concentrate on overseas automotive ventures." Yoon, 57, is a trusted ally who graduated from the same high school Kim did.

Kim's decision has shocked some employees, who worry about a potential managerial vacuum. But few Daewoo watchers believe the group will begin to drift. For starters, Kim's full-time presence in Europe will turn up the heat on competing auto makers. Kim, who spent nearly 250 days in Europe last year, wants to knit together his daring auto investments of nearly $3 billion (table).

Kim is convinced these low-cost manufacturing bases will allow him to dramatically undercut such rivals as General Motors, Ford, Volkswagen, and others in Western Europe. Daewoo is committed to investing an additional $2 billion in the next five years to improve those plants. Daewoo Motor's ultimate goal is to break into the ranks of the world's top 10 auto makers by making 2 million cars a year by 2000.

RETRIBUTION. Kim has an old score to settle with General Motors Corp. in particular. GM and Daewoo entered an alliance in the late 1980s, with the American giant buying 50% of Daewoo Motor. The venture fell apart in 1991 amid acrimony, and Daewoo was barred from the U.S. until 1996. That left Kim with little alternative but to focus on developing markets. Now it could be payback time, with GM's position in Europe a key target. "He wants to prove to GM that his strategy of concentrating in Third World markets does work," says one source close to Kim.

STRATEGIST *Kim will focus on cars in Europe*

Back home, Kim's departure could help rejuvenate the ranks of his group's management. When Daewoo announced its annual round of promotions in early January, nearly 100 younger managers were appointed to senior posts. Some of the newly appointed CEOs of Daewoo's companies are in their 40s, a bold move in Korea's highly seniority-based system. If Kim were still in place in Seoul, his dominating personality might discourage the younger managers from making more of their own decisions.

These managers are now expected to hammer away at the group's "global management" strategy with even greater vigor than before. That strategy calls for Daewoo to build hundreds of wholly owned subsidiaries and joint ventures in the emerging markets of Asia, Europe, and Latin America and realize total sales of $200 billion by 2000. Although that target may be unrealistically high, there's little question that Daewoo is going to continue to grow rapidly.

So although Kim will be in self-imposed exile, his move doesn't appear to reflect a blunting of Daewoo's global push. Company sources say Kim isn't likely to slow down appreciably. For three decades, he has never taken a single day off. "He won't be enjoying opera in Vienna, but watching operations," says Yoon. Most likely, the world hasn't heard the last from Chairman Kim.

By Laxmi Nakarmi in Seoul

DAEWOO'S MAJOR AUTO JOINT VENTURES

PLACE	VOLUME	DAEWOO INVESTMENT (THROUGH 1998) MILLIONS
UZBEKISTAN	100,000 CARS, 100,000 SMALL TRUCKS	$658
INDIA	200,000 CARS	$943
ROMANIA	200,000 CARS	$760
POLAND	250,000 CARS, 60,000 TRUCKS	$1,100
CZECH REPUBLIC	25,000 COMMERCIAL VEHICLES	NA

DATA: DAEWOO MOTOR CO.

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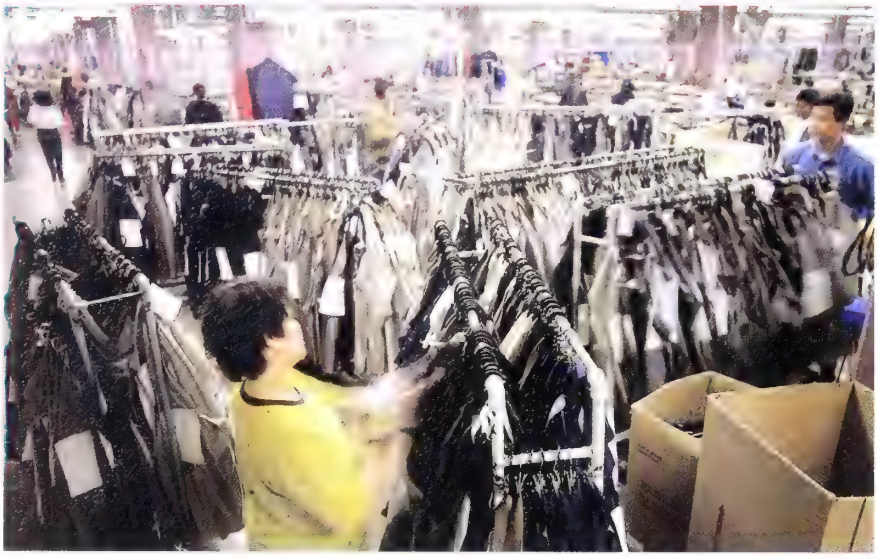


ON HOLD: *Many Montreal clothing makers will put off investments*

CANADA

BUSINESS IN QUEBEC IS VOTING WITH ITS FEET

As fears of sovereignty rise, companies may cut back–or flee

Just a few months ago, Jack Kivenko had ambitious expansion plans for his family's Montreal-based Jack Spratt Manufacturing Inc., which makes jeans for the Canadian market. But with the Quebec separatist movement on a seemingly unstoppable roll, those plans have been canceled. It's a common tale for the hundreds of clothing manufacturers that make Montreal Canada's rag-trade capital. "There's so much political uncertainty," says Kivenko with a sigh, "that I can't imagine anyone investing long-term dollars."

Such pessimism is running rampant as the ruling Parti Québécois prepares to install Lucien Bouchard as Quebec's Premier on Jan. 29. No wonder. Bouchard came within a hair of leading the separatists to victory in the Oct. 30 sovereignty referendum. Now that he's ascending to the French-speaking province's top job, many executives fear sovereignty is all but inevitable. "We are fighting what seems to be a losing battle," says Brian Neysmith, president of Canadian Bond Rating Service. Polls show support for independence has surged to 55%, up from 49.4% in October. "There is a real possibility that Quebec will be a sovereign country before 2000," Neysmith predicts.

Although Canadian federalists contend that it's too early to write off a united Canada, the growing possibility of sovereignty is hurting the Quebec economy. The province has underperformed Canada for two consecutive years. Last year, Quebec grew just 1.6%, down from 3.9% in 1994, the National Bank of Canada says.

As the gloom mounts, Quebec's housing industry has ground to a virtual standstill, as well. With fears growing that sovereignty would prompt an exodus of companies and individuals, housing starts there fell 43% in 1995, to 8,000, the lowest level since record-keeping began in 1965.

Business leaders fear this is just a taste of the bitter medicine to come. A new survey by the Conseil du Patronat, which represents Quebec's largest companies, reports that only 33% of Quebec executives feel economic conditions are "good or very good," down from 63% a year ago. "We have to accept the true seriousness of the risks we are running," argues Bank of Montreal Chairman Matthew W. Barrett. He predicts that a breakup of Canada would depress Quebec's economy by 7% "in the first year alone" and cost Canada up to $150 billion of lost growth over five years.

BOUCHARD: *Taking office with a 67% popularity rating*

Indeed, companies are already gearing up contingency plans. Canadian Pacific Ltd. has announced plans to move the headquarters of its CP Rail System unit from Montreal to Calgary. Although CP argued it was following its customers to western Canada, the move sent shivers through corporate Montreal. Bank of Montreal is also warning that it may move its head office out of Quebec if the province splits with Canada.

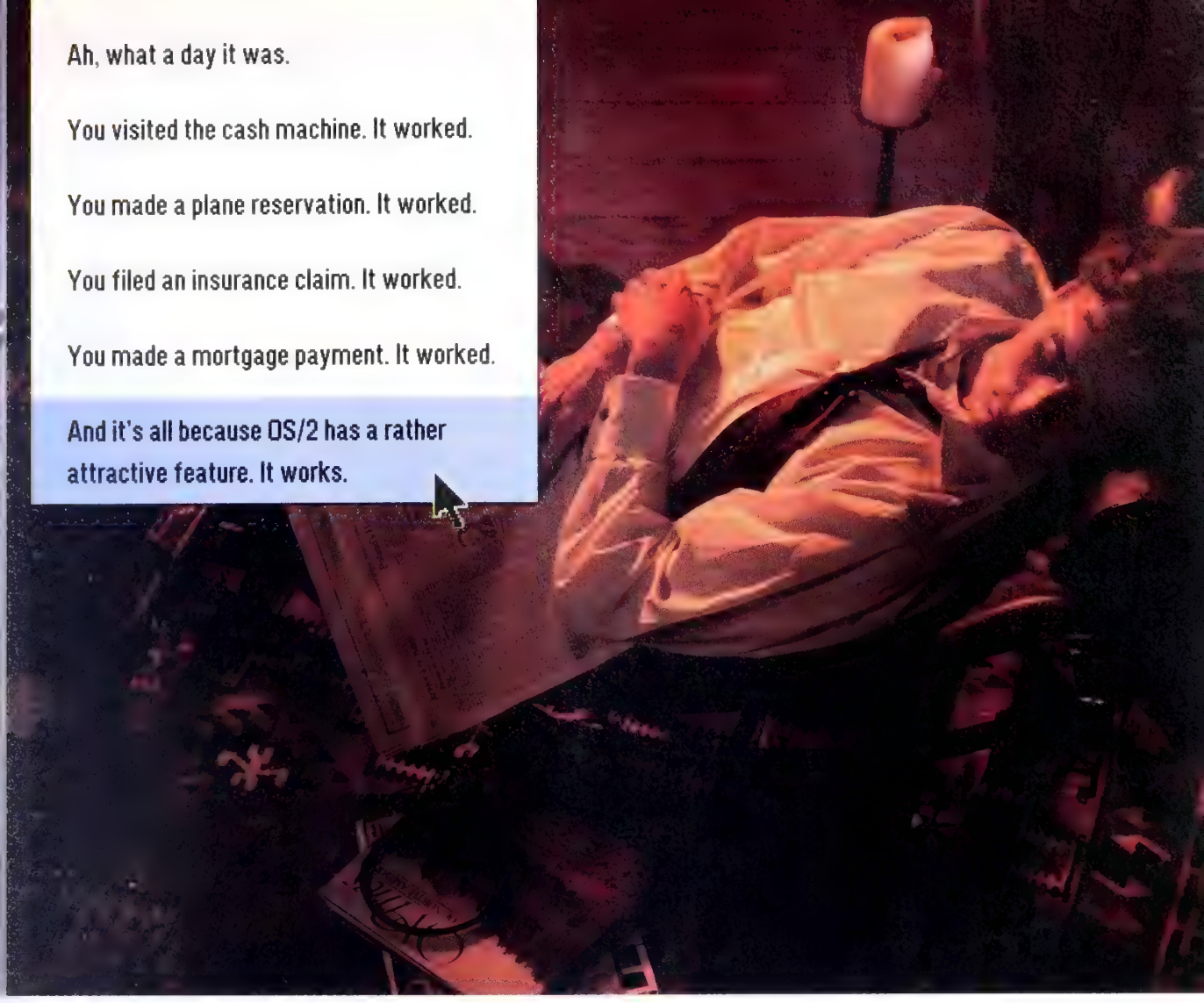
PLUNGING CONFIDENCE. Other companies chartered to do business in Canada, such as Air Canada Inc. and telecommunications giant BCE Inc., could follow. "You name me a company with pan-Canadian or North American interests now headquartered in Montreal," says Gordon Ritchie, chief executive of Ottawa-based trade consultants Strategico Inc., "and you've named a company looking at moving out."

Even companies such as General Motors Corp., which produces its entire output of Chevrolet Camaros and Pontiac Firebirds at its plant in Sainte Therese, Que., face uncertainty. No one knows how quickly an independent Quebec would be admitted to the North American Free Trade Agreement. "It would complicate our lives tremendously if we didn't have the free-trade agreement to ship duty-free into the U.S. and Mexico," warned GM of Canada President Maureen Kempston Darkes at the Montreal auto show on Jan. 9.

Such plunging business confidence has already caught Bouchard's attention. To buck up trust, he's promising his first priority will be a "vigorous housecleaning" of Quebec's bloated public sector. That's long overdue. Quebec's total debt burden is higher than that of any province except depressed Newfoundland, and Quebec is the only province that has yet to vigorously attack its deficit, now $3 billion. Bouchard also pledges to delay another referendum probably until next year.

But these measures don't address the fundamental problem: Bouchard's goal is to make Quebec a sovereign country. And he'll take office with a lofty 67% popularity rating, "the highest ever recorded" for a Quebec Premier, says pollster Jean-Marc Leger. No wonder business is hedging its bets.

By William C. Symonds in Montreal



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EDITED BY STANLEY REED

JAPAN: THE BANKING SCANDAL COULD HAMSTRING HASHIMOTO

Tokyo's normally placid political district is seething these days. Riot police are ringing the fortress-like walls of the Ministry of Finance. On Jan. 21, a right-wing group rammed a bus into the central gate of Japan's Diet building. Bullhorns now blare out anti-government slogans to throngs of angry demonstrators.

The government is feeling extreme heat from the public because of a proposed $6.8 billion rescue of seven bankrupt housing loan corporations, or *jusen*. A monster scandal seems to be brewing that could bog down the Japanese political system for months. Prime Minister Ryutaro Hashimoto, whom the ruling coalition brought in as a dynamic fresh face on Jan. 11, is in danger of being crippled in his first weeks in office.

What has infuriated taxpayers is the prospect that they will have to foot the bill for extraordinary negligence if not outright criminal activity. During the go-go late 1980s, the *jusen* went way beyond their original home mortgage businesses and lent wildly for office buildings, golf courses, and other risky deals. Some of the money went to *yakuza* criminal gangs (BW—Jan. 29). The regulators and mainline banks stood by and, mysteriously, did almost nothing to stop this activity. An incredible 89% of the *jusen's* $100 billion loan portfolio has gone sour.

PROTEST: *A bus crashed into the Diet*

The opposition leader, Ichiro Ozawa, has already jumped on the *jusen* affair as a vehicle to trash Hashimoto. The two men are likely to lead their respective camps in a general election later this year. Ozawa grilled Hashimoto in the Diet on Jan. 24, demanding that he drop the bailout.

If that happens, there could be major consequences for the big Tokyo banks. They have already agreed to forgive $60 billion in *jusen* loans. Now the bill could go up. Fuji Bank Ltd. and Hokkaido Takushoku Bank Ltd. are already planning to take big *jusen*-related losses in the fiscal year ending in March. And Moody's Investors Service lowered its rating on Sakura Bank Ltd. and Long-Term Credit Bank of Japan Ltd. on Jan. 23, citing debt problems related to the *jusen*.

CLIPPING WINGS. But there seems no stopping the mushrooming scandal. Hashimoto has agreed to a major Diet inquiry into the *jusen* problem. Before this is over Liberal Democratic Party stalwarts, ex-MOF bureaucrats, and other prominent members of the establishment are going to face serious embarrassment. Ozawa's aides are determined to expose links between Hashimoto's Liberal Democratic Party and the *jusen*. Ozawa's New Frontier party has set up a fax hotline for the public to send in tips.

Ozawa will also try to use the scandal to accomplish one of his pet goals: clipping the bureaucrats' wings. Already, Yoshitaka Murata, an ex-MOF career official, admitted on Jan. 9 that he received $190,000 in director's compensation from an Osaka-based real estate company that is deeply indebted to the *jusen*. Murata, however, has agreed to pay the money back. One question that Ozawa will be asking is what dozens of ex-MOF officials did to gain lucrative *jusen* jobs.

But whether Ozawa will be able to use the *jusen* affair as his ticket to power is an open question. The New Frontier chiefs also may have *jusen* ties that will come out in the probes. Ozawa is a pro but his party, says political lobbyist Dan Harada, "is absolutely no match for the entire brain trust of the LDP." Still, the *jusen* affair is at the very least going to further liven what was already looking like a stimulating political year in Japan.

By Brian Bremner in Tokyo

GLOBAL WRAPUP

VENEZUELA GETS OIL BUCKS

▶ Global oil heavyweights are scrambling to regain footholds in Venezuela two decades after the country nationalized its oil industry. International consortiums led by Mobil Oil Corp. and Conoco Inc. were among the winners in a sale of exploration tracts put on the block by cash-strapped state oil monopoly PDVSA in a week-long auction starting on Jan. 22. The sale is expected to trigger $1 billion worth of exploration. Despite tough terms, companies are drawn by Venezuela's track record as a major producer, its infrastructure, and relative political stability.

FIDEL DRAWS INVESTORS

▶ Continuing to end-run the American embargo, Cuba's President Fidel Castro recently signed two high-profile deals. WMC International Ltd., an Australian mining company, agreed to a 65-35 joint venture with Cuba's Commercial Caribbean Nickel to tap the island's huge nickel reserves in a transaction valued at $500 million. WMC joins about 20 other foreign mining companies in Cuba. Nickel is the island's third-largest hard currency generator, behind sugar and tourism.

Cuba's tourism sector also got a boost with the announcement that Club Méditerranée will market and manage a 300-room resort scheduled to open in November. Such deals have helped Cuba turn a corner in its economic struggle. After falling about 35% between 1989 and 1993, gross domestic product is now forecast to register 5% growth this year, double last year's rate.

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MEDICINE

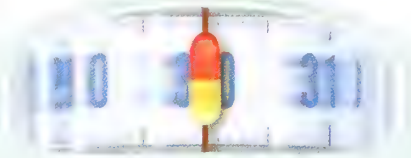
IS THERE A CURE FOR OBESITY?

Could be–and drugmakers are determined to find it

For obesity sufferers, it's been a painfully long dry spell. The last new drug to treat the condition was approved in 1974, and it could only be used for three months. Since then, restrictive diets and exercise were the only treatment options for the 60 million or so obese adults. It's a strategy that has failed. Obesity costs Americans a staggering $100 billion in healthcare costs and weight-loss schemes, according to the U.S. Surgeon General. Now, finally, there's hope for a little relief.

The Food & Drug Administration is considering two promising new treatments for obesity and a third is expected in a year or so. These drugs are not magic bullets. In clinical trials, they achieved only about a 10% reduction in weight even in conjunction with diet and exercise regimens. There's no guarantee that the drugs will work long term, and the FDA is likely to set high standards for approval. But the drugs' appearance is the first clear sign that such companies as Hoffmann-La Roche Inc. and Knoll Pharmaceutical Co. are pursuing what could be a $3 billion or more market. "We are seeing drug companies that we've not seen in years," says Dr. Susan Z. Yanovski, who heads the National Task Force on the Prevention and Treatment of Obesity.

The big change is related to a fundamental shift in how obesity is viewed. Doctors have concluded that obesity, once deemed a lack of will, is a chronic illness much like diabetes and must be treated long term. The FDA is following suit. All drugs up for approval must be safe and effective for at least a year, and most states are rescinding their three-month restriction on new drugs.



A Timetable For Fat-Fighting Drugs

For the first time in some 20 years, a drug to treat obesity is up for FDA approval. With a surge in research, more are likely to follow.

IN TWO YEARS

DEXFENFLURAMINE Decreases appetite by promoting the release of serotonin and preventing its uptake in the brain. *Interneuron with Wyeth-Ayerst Laboratories*

SIBUTRAMINE Also reins in appetite by preventing uptake of serotonin, as well as another brain chemical called noradrenaline. *Knoll Pharmaceutical*

ORLISTAT Promotes weight loss by blocking fat digestion. *Hoffmann-La Roche*

IN THREE TO FIVE YEARS

BETA-3 ADRENERGIC AGONISTS Treat obesity by speeding up the body's energy expenditure. *Wyeth-Ayerst Laboratories*

CCK-A PROMOTER CCK-A is a hormone found in the gut that seems to inhibit eating. The idea is to enhance its effect. *Astra, Glaxo-Wellcome*

IN FIVE TO TEN YEARS

OB-PROTEIN Found naturally in the body, this protein reduces appetite and speeds up fat-burning in mice. *Amgen*

OB-RECEPTOR Researchers are designing drugs that would help convey the message normally delivered when the Ob protein binds to its receptor. *Hoffmann-La Roche w/Millennium*

NEUROPEPTIDE-Y This brain chemical seems to promote feeding behavior in animals. Blocking its effects could reduce appetite. *Neurogen with Pfizer, Synaptic Pharmaceutical*

DATA: DECISION RESOURCES AND BUSINESS WEEK

This view of obesity reflects a wave of recent findings. One key development was the discovery last March of the so-called Ob-gene and its related protein, leptin. Some 20 genes may play a role in obesity—and more are expected. Scientists are hunting down brain chemicals that regulate hunger, and they're exploring why one person burns fat faster than another. The result is a clearer picture of what causes obesity and how best to treat it. "New treatments will be designed on a rational basis having to do with our knowledge of how body weight is regulated at the molecular level," says Dr. Jeffrey M. Friedman, a researcher at the Howard Hughes Medical Institute at Rockefeller University in New York.

The first new generation of drugs is just beginning to meet this criterion. The drug closest to market, dexfenfluramine, made by Interneuron Pharmaceuticals Inc. in Lexington, Mass., already is available in 65 countries. It reduces appetite by increasing the levels of serotonin in the brain. Recommended by an advisory committee to the FDA, it now awaits approval. Next in line is sibutramine, which was submitted to the agency in August and is made by Knoll. It prevents uptake of serotonin as well as another brain chemical called noradrenaline, which is involved in metabolism.

GUT REACTION. The third drug nearing the market is Roche's orlistat, which prevents the intestines from absorbing about one-third of the fat a person consumes. The drug is in late clinical trials and could be approved within two years, says Dr. Arthur Campfield, a research leader in the department of metabolic diseases at Roche.

Beyond these early entries, a handful of other drugs may be ready within five years. Drugs called beta-3 adrenergic agonists work by increasing the body's energy expenditure. Wyeth-Ayerst Laboratories Inc. already has one in clinical trials. Another approach is to look at compounds that control when people are satiated. An example is CCK-A,

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Equity Income	★★★★★	★★★★★	★★★★	★★★★★
Growth & Income	★★★★	★★★★	★★★★	★★★
Growth Stock	★★★★	★★★★	★★★★	★★★
Mid-Cap Growth	★★★★★	★★★★★	–	–
New America Growth	★★★★	★★★★	★★★★★	★★★★
New Era	★★	★★★	★★	★★
New Horizons	★★★★	★★★★★	★★★★★	★★★
OTC	★★★	★★★★★	★★★★	★★
Science & Technology	★★★★★	★★★★★	★★★★★	–
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a hormone produced by the gut that tells the brain a person is full. Researchers at Astra Arcus USA in Rochester, N. Y., are testing a drug that can boost this effect in humans.

Others are working on neuropeptide-Y, a substance in the brain that causes rats to overeat. The idea is to block its effect in people. Neurogen Corp. in Branford, Conn., along with Pfizer Inc., filed on Dec. 13 for permission to begin trials of such a drug. Synaptic Pharmaceutical Corp. in Paramus, N. J., also is pursuing an NPY blocker.

TOUGH SELL. Clinicians are most excited about the potential payoff from genetics research. Since discovering the Ob-gene last year, researchers have found that the Ob-protein, or leptin, is released by fat cells in the body. It travels to the hypothalamus, at the base of the brain. There it binds with the Ob-receptor and touches off a chemical cascade that suppresses appetite. Leptin also may tell the body to burn more fat.

So far, though, leptin's function in humans is murky. Amgen Inc. is hoping to inject people with the protein to see if they lose weight. The sticking point is that some obese people already have high levels of leptin in their bloodstream. Giving them more may not have an effect. "I think the jury's still out on whether leptin could be a drug or not," says Friedman, leader of the team that isolated the Ob-gene and -protein.

Campfield's group at Roche is focusing more on the Ob-receptor. The company, with Millennium Pharmaceuticals Inc. in Cambridge, Mass., found the receptor in December and determined that leptin does bind to it. The problem, says Campfield, seems to be getting the fat-fighting message through to cells in the hypothalamus. His group is working on finding small molecules that can facilitate this connection. "I think we could get lucky here," says Campfield.

Finding a profitable drug likely will require a little luck. Researchers believe obesity results from a number of genetic and environmental factors. The hope is that doctors will one day have an arsenal of drugs to tailor treatment.

There is still doubt about how effective any one treatment can be. Eating is an instinct: Use a drug to interfere with one pathway and another might take over, says Dr. Richard L. Atkinson, director of the Beers-Murphy Clinical Nutritional Center at the University of Wisconsin-Madison. "There may be a whole lot of signals telling the body it should be fatter."

Another hurdle for obesity drugs is the FDA. The agency released preliminary guidelines on these therapies in 1994, and they still are "evolving," says Dr. Leo Lutwak, an FDA medical officer. Questions remain as to how long studies must last and what amount of weight loss is optimal. Some FDA advisers want the drugs to also reduce the incidence of such obesity-related problems as diabetes or hypertension.

Because obesity isn't directly life-threatening like AIDS or cancer, the risk of taking a drug long term is weighed carefully against the benefit of weight loss. This hesitancy makes some weight-loss advocates impatient. "I don't think approval of antiobesity drugs falls on a very sympathetic advisory committee or FDA," says committee member Judith S. Stern, a professor of nutrition at the University of California at Davis.

Perhaps sensing this, Eli Lilly & Co. withdrew its obesity drug Lovan—a Prozac-like compound—from review at the FDA, citing costs required for two-year studies. Dexfenfluramine was narrowly recommended amid much dissent, including worries about its effect on the brain. It has opponents even among some obese people.

Still, this level of controversy is inevitable in such a new area, says Richard E. Gammans, vice-president for clinical research at Interneuron. "We're at the stage now in obesity drugs that we were with drugs for depression 15 years ago." It could take years before obesity suffering is truly alleviated.

By Naomi Freundlich in New York, with Colleen M. Sauber in Boston and John Carey in Washington

FOR SOME, IT'S BETTER SAFE THAN SVELTE

Lynn McAfee has reason to be wary of obesity drugs. By the age of 6, McAfee was taking amphetamines, digitalis, and diuretics to treat her weight problem. The drugs—given to millions of overweight people—took a toll. "Many of us were very seriously damaged," she says. McAfee, now 46 and a director of the Council on Size & Weight Discrimination, an advocacy group, had to overcome amphetamine addiction as well as psychological trauma.

ACTIVIST McAFEE: *She vows to attend new drug hearings*

This history explains why McAfee and other advocates, such as the National Association to Advance Fat Acceptance (NAAFA), oppose approval of the latest obesity drug, dexfenfluramine, made by Interneuron Pharmaceuticals Inc. Even though the drug is available in 65 countries, McAfee says she is troubled by reports of brain toxicity in monkeys and the increased incidence of a very rare disorder—primary pulmonary hypertension (PPH), which affects blood vessels feeding the lungs.

McAfee recognizes that many obese people are clamoring for these new drugs. But she worries that society is biased against overweight people, leading to a weight-loss-at-any-cost attitude and approval of dangerous drugs.

"DETERMINED." Bobby W. Sandage Jr., executive vice-president for research and development at Interneuron, doesn't see dexfenfluramine as harmful. He says that neurotoxicity was seen in animals only at doses greater than 30 times those given humans. In year-long tests on humans, there were no adverse brain effects. As for PPH, Sandage says the drug, along with obesity itself, does increase the incidence slightly. "Risk-benefit is still in favor of benefit," he says.

Assurances aside, McAfee says she will personally show up at the Food & Drug Administration for every obesity drug review possible. Her goal: "We're determined that we're not going to pay again for drugs that harm us rather than help us." That may mean the FDA decision could be political as well as medical.

By Naomi Freundlich

BusinessWeek

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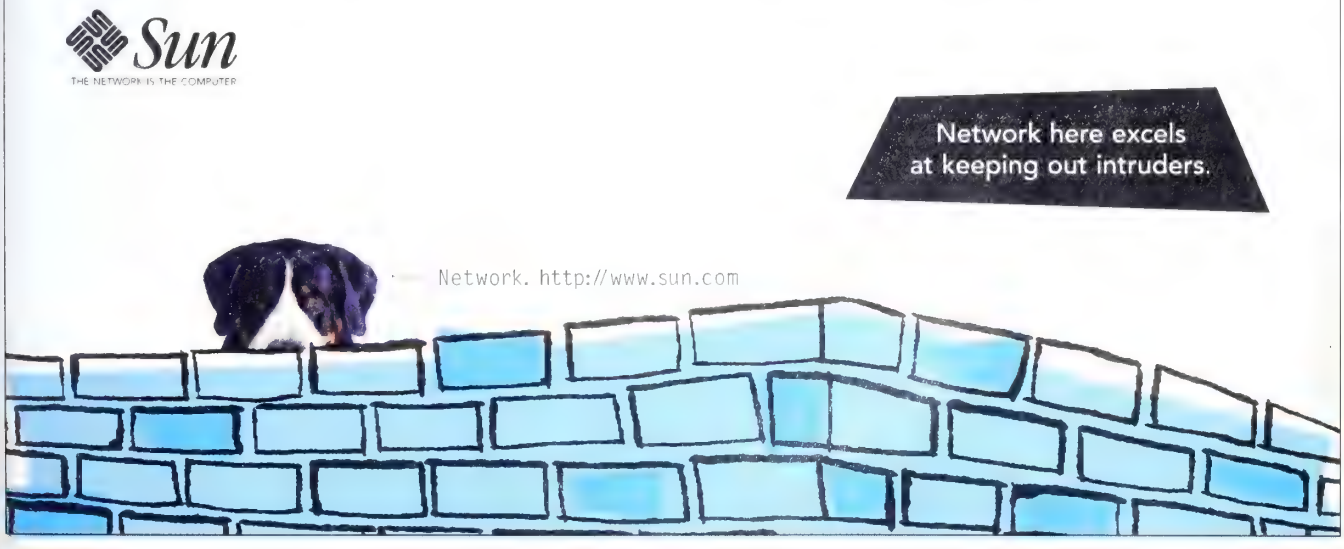
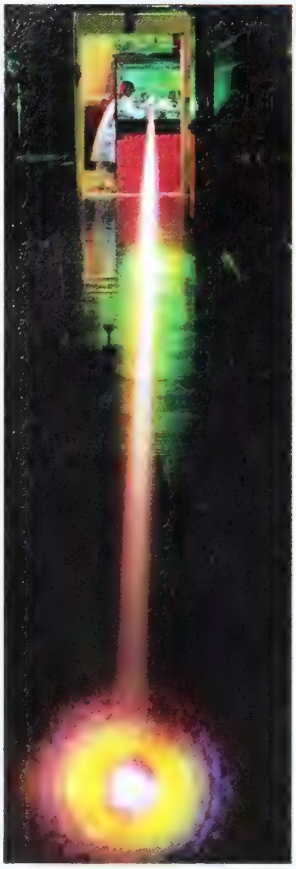


EDITED BY NEIL GROSS

A NEW GAUGE FOR AIDS TREATMENTS

THE EVALUATION OF AIDS therapies is a tricky business. Waiting until a drug regimen shows a clear-cut effect in extending life or reducing secondary infections may take years. And measures of a treatment's effectiveness now in use are less predictive than doctors would like. For example, it's clear that a big drop in the numbers of an immune system cell called CD4 is a bad sign. But a small, drug-induced rise in CD4 counts doesn't necessarily help. Doctors and AIDS activists think there may be a better gauge of a patient's progress: directly measuring the amount of virus—the viral load—in the body.

Now there's firm proof that it works. To evaluate a new AIDS drug, Pharmacia & Upjohn Co. is using a sensitive test, polymerase chain reaction (PCR), to measure viral load. The preliminary results, announced on Jan. 17, are striking. Subjects who started the trial with less virus took longer to get sick than those harboring more HIV. And those in whom the drug cut viral levels 90% were five times less likely to die or progress to more serious stages of the disease. That means the amount of virus is "a very powerful predictor," says AIDS activist Ben Cheng of Project Inform. Clinicians and activists are now pressuring insurers and HMOs to pay for PCR viral load tests, which cost between $125 and $250 each, as part of normal patient care.



'CHIRPING' LASERS THAT CAN SMASH ATOMS

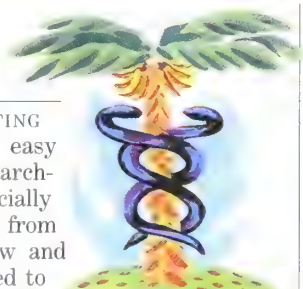
EVEN BEFORE THE GIANT, $11 billion Superconducting Super Collider (SSC) was scrubbed in 1993, an international band of scientists was chasing a much cheaper alternative: an atom-smasher small enough to sit on a laboratory table and allow any university lab to probe the frontiers of subatomic physics.

Well, splitting atoms on a table is no longer the stuff of distant dreams. Gerard A. Mourou, director of the University of Michigan's Ultrafast Optical Science Center, is convinced that semiconductor lasers can match the SSC's power—or even top it. The key is using one laser pulse to drill a hole through a gas, creating a plasma tunnel that serves to guide subsequent laser pulses. A following pulse can then snare electrons in its energy field and push them to atom-smashing speeds.

Accelerating an electron to speeds fast enough to split an atom is a function of distance. In normal accelerators, it takes miles of electromagnets to get up the necessary speed and energy. But with so-called "chirping" lasers that Mourou helped pioneer, "we could achieve SSC energies in just a few meters," he says. Chirping involves stretching a laser pulse so its energy can be amplified many times, then compressing it into an ultrashort, ultrapotent blast. Before the plasma tunnel, there was no way to prevent these pulses from rapidly diffusing. Optical fibers wouldn't work because chirped pulses would vaporize the glass.

In the current setup, the pulses travel only a centimeter. By yearend, Mourou hopes to extend the distance to several centimeters. And scientists are already working on plasma tunnels many meters long (photo).

BEULAH, PEEL ME A VACCINE



IT MAY NOT BE LONG BEFORE GETTING vaccinated against a disease is as easy as eating a banana. British researchers say they've found a commercially viable way of growing medicines from plants—an advance over the slow and costly fermentation techniques used to produce most vaccines today. Axis Genetics, a small Cambridge biotech outfit, first infects the plants with genetically engineered viruses. These in turn produce structures in the plant leaves that contain biologically active proteins and protein fragments, called peptides, that can be used as vaccines.

The first peptides produced this way were small and of limited usefulness. Help came last July from scientists at the Scottish Crop Research Institute (SCRI) who were experimenting with the same technique. They altered the shape of the virus particles using an animal protein "overcoating." The plants then began producing proteins 10 times the size of earlier peptides. That increase makes them suitable for a variety of medicines, says Mike Smith, a professor at SCRI.

INNOVATIONS

■ The U. N. estimates that there are 100 million land mines buried in 64 countries around the world. To help locate them, scientists at the Army Research Laboratory and Mercury Computer Systems Inc. in Chelmsford, Mass., are testing new mathematical algorithms embedded in computer chips. Radar systems equipped with the chips might be able to distinguish buried pipes from bombs.

■ British glassmaker Pilkington PLC says it has a new, environmentally friendly technique for making mirrors: It sandwiches together thin layers of silicon and silica coatings, thus reducing dependence on lead-based paints and other harmful chemicals.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwfeb@businessweek.com

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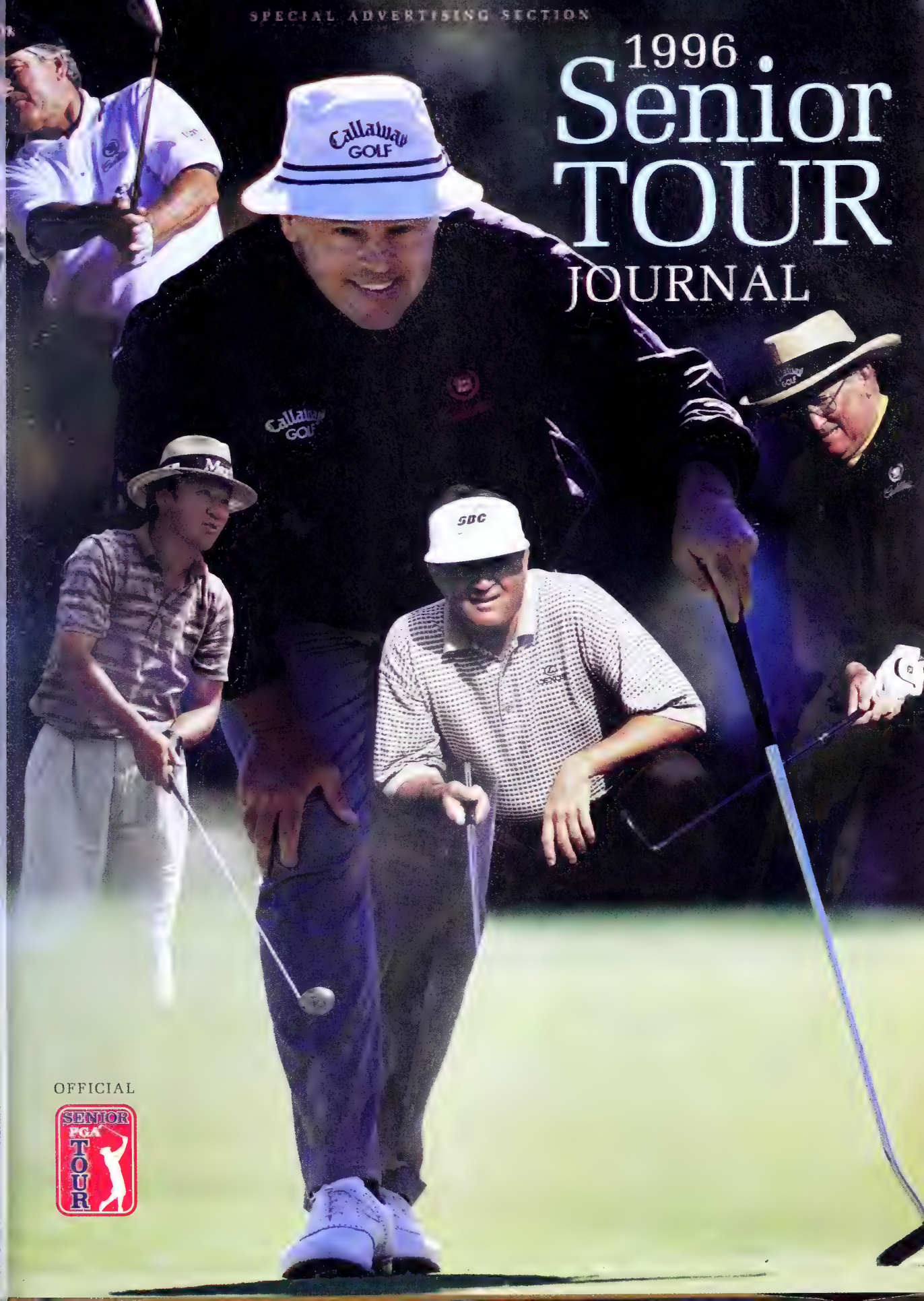

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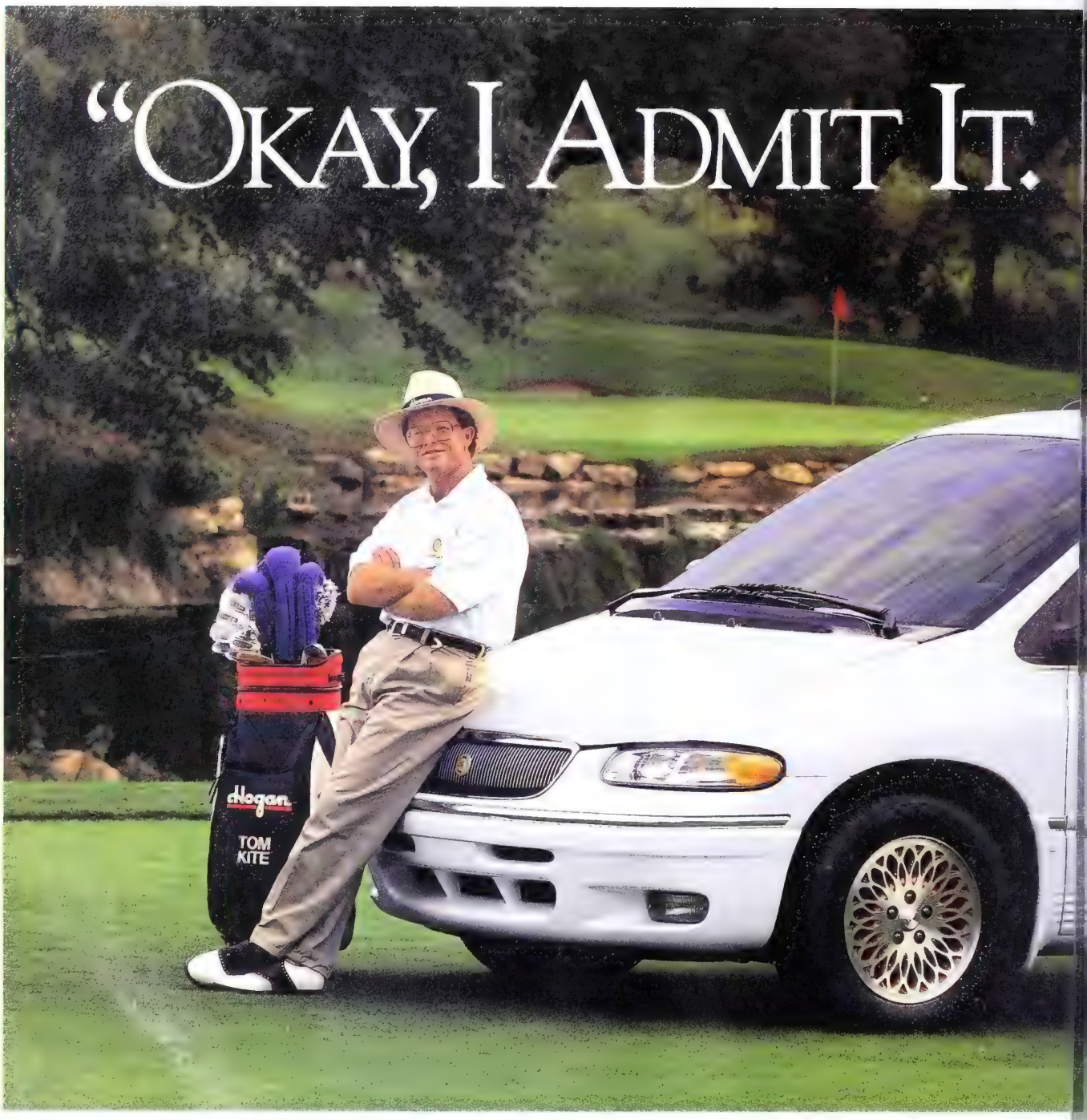
"Okay, I Admit It.



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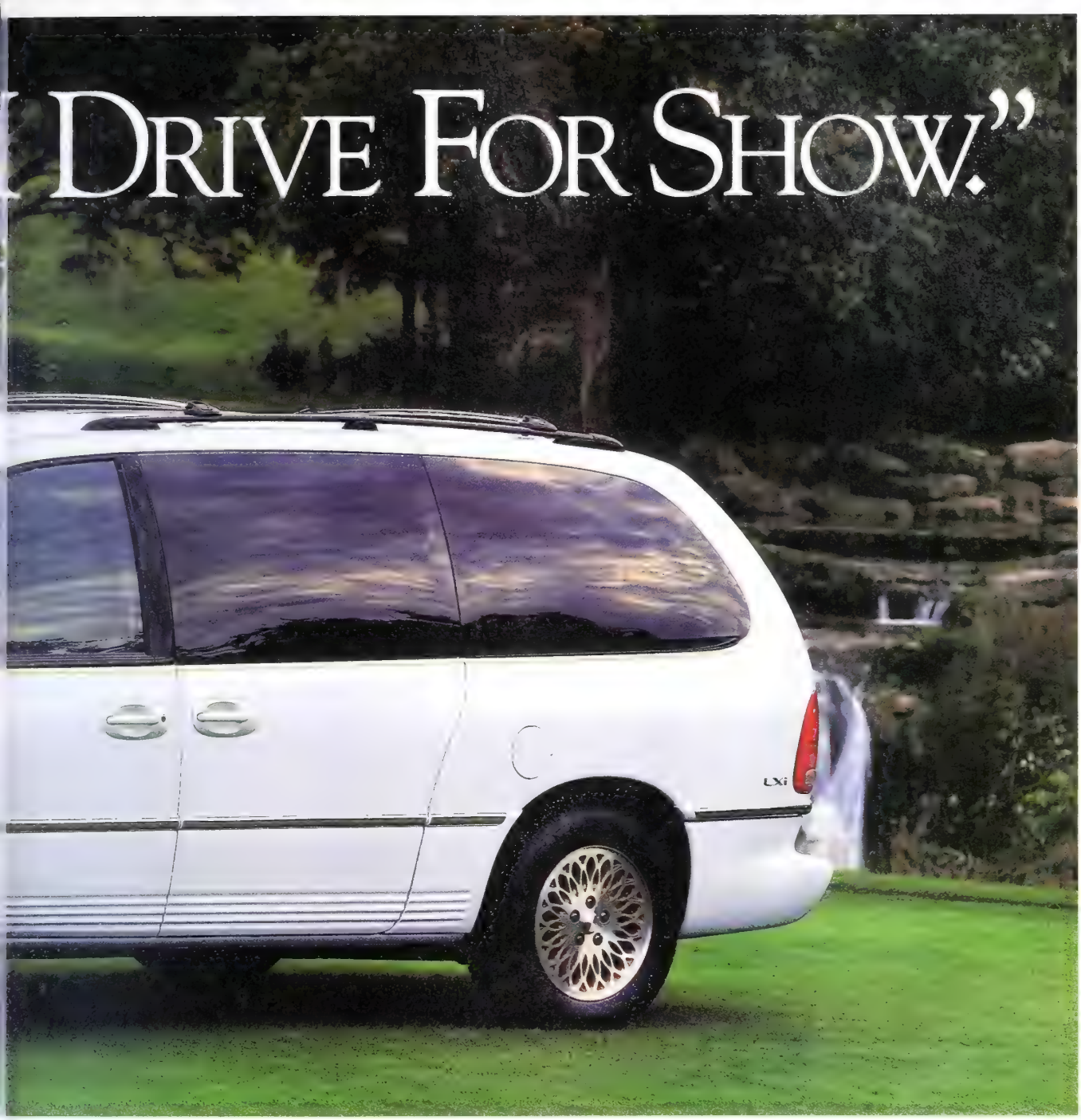

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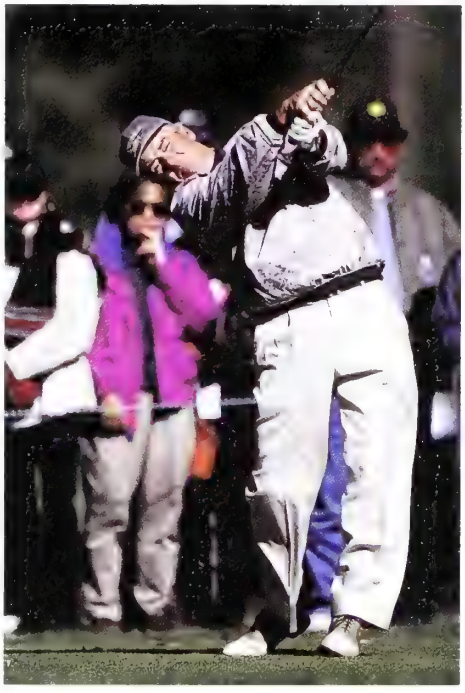
STAN BADZ - PGA TOUR

SAM GREENWOOD - PGA TOUR

Seniors Make Their Mark


SAM GREENWOOD - PGA TOUR

By Ron Green

The pages on the calendar turn, hair grays, lines deepen, swings grow shorter and less certain, and quietly, unwittingly, champions are nudged aside to make way for new champions. It is inevitable. It is reason for regret, but also reason for rejoicing.

Their tastes in food, books, TV, movies, clothing, politics, philosophies and a multitude of other things are as diverse as their faces and their golf swings. But they have this in common: they are the current rulers of the Senior PGA TOUR.

They were the Fab Five of 1995.

They can get the ball down the fairway and into the cup, and they did it better and/or more often than any of the others last year. They were the five leading money winners of 1995, all topping the million-dollar mark, in their order: Colbert, $1,444,386; Floyd, $1,419,545; Stockton, $1,415,847; Murphy, $1,241,524, and Aoki, $1,041,766. Among them, they won 15 of 38 official Senior TOUR events and were second or tied for second 21 times. They banked $6,563,068, close to 20 percent of the more than $32 million in Senior TOUR purses.

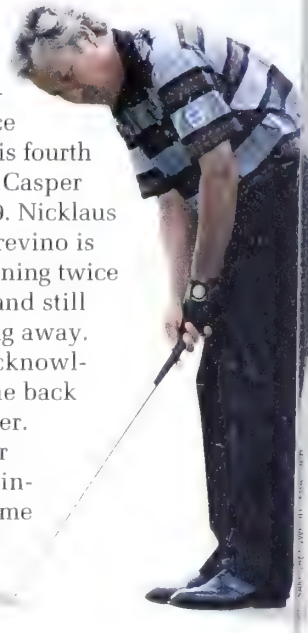
A good measure of how tough it has become is tournament victories.

They did all that despite occasional forays onto the TOUR by Jack Nicklaus, the arrival in June of three-time U.S. Open champion Hale Irwin, the fact that Lee Trevino is still out there stalking trophies, a super rookie season by Bruce Summerhays and a career year by J.C. Snead, among other obstacles.

A good measure of how tough it has become is tournament victories. Nobody won more than four tournaments in 1995. It was the first year since 1984 that someone didn't win at least five. In 1985, Peter Thomson won nine. In 1987, Chi Chi Rodriquez won seven.

They fill space once owned by Don January, Miller Barber, Gene Littler, Orville Moody, Lee Elder, Thomson, Bob Charles, Bruce Crampton, George Archer, Don Bies, Al Geiberger, Mike Hill, Dale Douglass, Charles Coody.

And, of course, once owned by Hall of Famers Arnold Palmer, Gary Player, Billy Casper, Jack Nicklaus, Trevino and that irrepressible showman, Rodriguez.


SAM GREENWOOD - PGA TOUR

Palmer still plays and thrills the crowds – but doesn't win anymore. Player won once in 1995. It was only his fourth victory in the 1990s. Casper hasn't won since 1989. Nicklaus plays infrequently. Trevino is still playing well: winning twice in 1995 and still chattering away. But, at 56, even he acknowledges that he is on the back nine of his great career. Rodriguez, the Senior TOUR's most entertaining player and a 22-time winner, hasn't picked up a trophy since 1993.

The Fab Five of 1995 may like different foods, books, TV, etc., but there has to be something they all have that brought them to the top.

"They play a lot and work hard," said Trevino. "Some of them are better now than they were 25 years ago because they're working more at it."

J.C. Snead, who flirted with the top five before finishing sixth on the money list, said, "They're all very good putters. Obviously, they can play pretty good, too. It's not all done with the putters. Stockton hits the ball better now than he ever has because he's learned more about his swing and proper fundamentals."

Stockton says, to be in the top five, "You have to have an all-around game. All of the players at the top are going to be good putters. You have to have imagination. You have to be a positive person, look at the bright side all the time."

Trevino has been the best regular player on the Senior TOUR since 1990, when he has been healthy. But Floyd, who joined the TOUR in late 1992, may have overhauled him now. In 1994, Floyd played 20 senior events and averaged winning $69,138 per event. In 1995, he played 21 senior events and his average winnings were $67,597.

SAM GREENWOOD - PGA TOUR

At that rate, you might think he would choose to play more, but he says he'll stick to that schedule.

"I don't have time to play more," he said. "I enjoy playing, but I have a course design business and I have a family life to lead, so I can't play every week. It's not the quantity of play that makes the player, it's the quality."

All of the players at the top are going to be good putters.

SAM GREENWOOD - PGA TOUR

Floyd has changed little since moving from the PGA TOUR to the senior circuit. He said he still practices as hard, but has put more emphasis in practice on his short game.

"I used to spend about half the time on the scoring part of my game," he said. "Now it's 60-40, maybe 65-35, the bigger part being on the scoring shots."

Floyd played straight through, simply lapping over from the PGA TOUR to the Senior TOUR, never missing a beat. He still plays in several PGA TOUR events each year.

Whereas Floyd was literally a Hall of Famer when he arrived on the Senior TOUR, Colbert made himself a top-notch player, redesigning his life to make way for the player that was in him. He finished last year by winning the Energizer SENIOR TOUR Championship in Myrtle Beach, SC to clinch first place on the money list and to win the Cadillac Series, in which points are awarded according to finish in TOUR events televised by ESPN.

Colbert had a fine career on the PGA TOUR, winning eight times, but he never won a major. His finest hour came in 1983

"We all have a competitive nature," said Murphy. "We have a desire to do well. On the golf side, you have to point at the putters. After that, putting the ball in play and being good around greens."

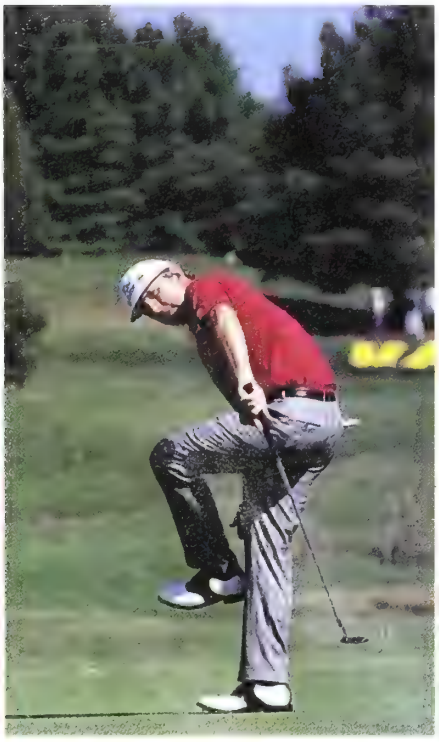
when, at age 43, he beat Fuzzy Zoeller in a playoff to win the Colonial National Invitation and notch his second victory of the year.

But then he left the TOUR, developed a successful golf course management business and became a TV commentator. Once he got into senior golf, though, he cleared the decks.

Irwin undoubtedly will push his way into the top five in 1996.

"I gave myself every opportunity to be as good as I could for as long as I could," said Colbert. "I hired a full-time trainer. I stretch twice a day and work out four times a week. I wear magnets on my back to cope with a problem I have, and I haven't had a flare-up in two years."

As with Colbert, Stockton abandoned tournament golf for several years before turning 50. In the 1980s, he became known as the "King of the Corporate Outings," averaging more than 90 days a year mixing business and professional people with golf.



SAM GREENWOOD

"I'm sure I would have won more tournaments if I had played more," he said, "but the question would have been how my kids turned out. I'm so proud of my kids (David, born in 1968, now a PGA TOUR player, and Ronald born in 1970 and also involved in golf). I have no regrets about giving up my competition for a number of years and doing corporate outings, because it gave me a lot of time at home."

He had a splendid PGA TOUR career, winning nine times, including two PGA Championships. In 1991, he captained the U.S. Ryder Cup team, devoting most of his time to promoting that event. He intended to go back to his corporate outings, but his captaincy gave him a positive feeling about himself that he hadn't expected.

He wasted no time in becoming a Senior TOUR star, winning the FORD SENIOR PLAYERS Championship in 1992, his first full year out. He has since won 13 more (through 1995), plus two money-winning titles and a Player of the Year award in 1994.

"I feel good about what I've accomplished," Stockton said. "I think I've helped the Senior TOUR. It's great competition. You can't ask for anything better. I'm still having fun. It's great."

Aoki, whose home is Tokyo, played the PGA TOUR for 10 years, winning once when he holed a 128-yard wedge shot from the rough for an eagle on the last hole to leapfrog over Jack Renner in the 1983 Hawaiian Open. By the end of 1995, he had won four times on the Senior TOUR since turning 50 in 1992.

He's long off the tee. But the strongest part of his game is his putting, which he does by setting the heel of a Bullseye-style putter on the grass and turning the toe up at about a 45-degree angle before making his stroke.

He credits his rise to the top five to being more relaxed, having gotten to know his fellow players more and learning to speak a bit more English.

His caddie, John McCready, said, "He's got no weaknesses. He's a very strong driver, and his short game is awesome. He has fun out there. He genuinely enjoys playing the game.

"And he may be a little more focused now than he was earlier."

Aoki had a scoring average of under 70 in '95, led everybody in putting, was top 10 in greens hit in regulation and total driving, and was No.2 behind Floyd in the all-around category.

Which explains, in part, why he said, " I like the Senior TOUR. I'm very relaxed. Everybody's nice, friendly. I feel good."

Irwin undoubtedly will push his way into the top five in 1996. He almost made it in 1995, though playing only 12 tournaments. He finished 10th in money with $799,175, which had been a goal.

"All in all, it's been a fabulous start to my Senior TOUR play," he said. "The Senior TOUR is great. I'm a proponent. My future's out here."

Irwin won a PGA TOUR event as recently as 1994, when he captured his third MCI Classic in Hilton Head, SC. He won his third U.S. Open in 1990. He has remained extremely fit and has kept his golf sharp.

Eligible to join him and the others in 1996 are Frank Conner, Bob Eastwood, Grier Jones, David Graham, Gil Morgan, John Schroeder and Hubert Green.

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TPCs: Getting ready for the Senior PGA TOUR

By Chris Smith

Operational details are well orchestrated for the Las Vegas Senior Classic in April, typical of all five Tournament Players Clubs playing host to Senior PGA TOUR events.

Some adjustments are required for tournament week, including the maintenance schedule. Fairway mowing, for instance, is shifted from pre-dawn to the afternoon following play, allowing the crew to concentrate on greens, tees and bunkers during the early morning, prior to the start of each round.

At the TPC at Summerlin in Las Vegas, though, the afternoon shift involves one slight hitch. Consequently, superintendent Collier Miller takes on an additional role that he easily could do without. But it's necessary.

What players and spectators see is the culmination of months of planning

Due to the location of Summerlin's maintenance facility and the configuration of the golf course, a fleet of riding mowers must negotiate a busy public road to get to their assigned holes in a timely manner.

It falls upon Miller, then, to step into the road and direct traffic. "I don't look forward to that time of day," acknowledged Miller, who repeats the procedure in October during the PGA TOUR's Las Vegas Invitational.

Playing host to a professional golf tournament is no simple matter, particularly one of the magnitude of a PGA TOUR or Senior TOUR event. What players and spectators see is the culmination of months of planning and, hopefully, the successful execution of behind-the-scenes coordination between the clubhouse, food & beverage and maintenance operations.

Leading into tournament week, trucks rumble in with tons of equipment, corporate tents and skyboxes begin to spring up and miles of cable are laid throughout the grounds. Plans are made to coordinate service in hospitality areas as well as the clubhouse, plus there's consideration for increased merchandising. And once the tournament arrives, the club suddenly is engulfed by thousands of spectators, all with their own agenda of what to do, where to go and what to buy.

This said, the TPCs have proven themselves as model operations for golf tournaments. Besides Summerlin, host clubs on the Senior TOUR are the TPC of Michigan in Dearborn, site of the FORD SENIOR PLAYERS Championship; the TPC at Piper Glen in Charlotte, host to the PaineWebber Invitational; the TPC of Tampa Bay, site of the GTE Suncoast Classic, and the TPC at Prestancia in Sarasota, site of the American Express Invitational Presented by *Business Week*.

Fact is, short of the necessary planning and tweaking, these facilities essentially remain tournament-ready throughout the year.

Scheduling change is part of the system. During tournament week, the maintenance crew at Summerlin starts mowing the greens and tees as early as 4:30 a.m. and also sets pins and rakes bunkers. This work is completed by 9 a.m. It then typically returns to the course at 3 p.m. to mow fairways, fill divots, and roll and water the greens.

PGA TOUR ARCHIVES

The TPC of Michigan in Dearborn depends on member and guest satisfaction for success

It's essentially the same for all five TPCs with tournaments on the Senior TOUR. Even when the tournament is the prestigious FORD SENIOR PLAYERS Championship, one of the Senior TOUR's major championships.

"We try to prepare the course on a daily basis so there isn't a great deal of change prior to the tournament," said TPC of Michigan superintendent Mike Giuffre. "Our biggest challenge really is weather-related. For the last three years, we have had heavy storms blow through the course during the tournament. That is where all of our time and effort has gone, bringing the course back to playable condition."

The TPC of Michigan has bentgrass greens, which require special care due to the summer heat and number of mowings. "We do a lot of hand-watering," Guiffre explained. "We don't want to get the course too soft, and we want the greens consistent throughout the high, low or level spots."

The general preparedness for tournament week holds true for the clubhouse operation, where the biggest changes come in temporary staffing and increase in merchandise inventory and food & beverage.

"Because of the philosophy of standards we expect to meet at each TPC, you see the same look in terms of quality presentation," said Wayne White, General Manager of the TPC at Piper Glen. "Go from one TPC operation to another, and you see the same setup of operation. The senior players say they look forward to playing the tournaments at the TPCs because of this excellence."

Each department has a checklist of things to do leading up to tournament week. White's own lengthy list is set in motion four months prior to the event, held the week after Las Vegas.

"You really have a different focus when the tournament comes in," said Jack Morrison, General Manager at Prestancia, which previously played host to the Chrysler Cup. "As you move away from the day-to-day routine with food & beverage and the golf operation to prepare for thousands of people coming to the property and the traffic through the golf shop, the functions remain the same. It's just a different concentration due to the number of people on property. So the real change comes with the numbers of people with whom you are dealing." And once tournament week ends?

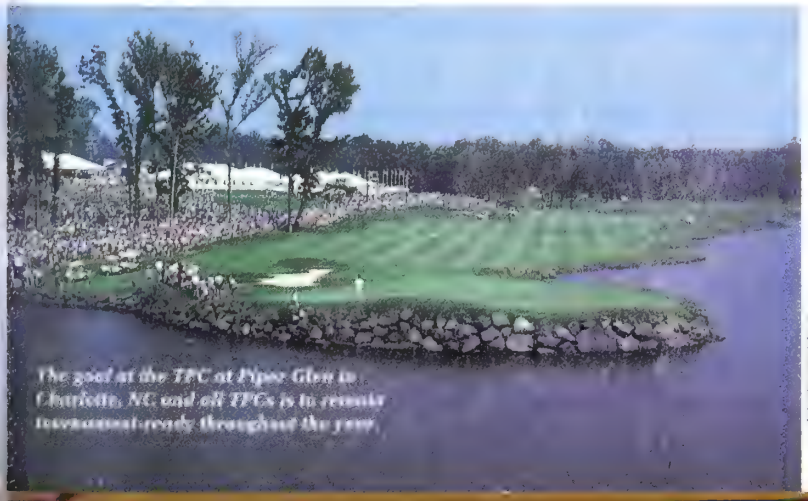
PGA TOUR ARCHIVES

A lot of time and effort keeps the TPC at Prestancia in Sarasota, FL in playable condition.

"We try to prepare the course on a daily basis so there isn't a great deal of change prior to the tournament."

"We have a philosophy," said Allen Jones, General Manager and Director of Golf at Summerlin. "When we open back up for play after the tournament, we take the pros' names off the lockers and take the banners down. Other than the large tents on property, it's the same operation."

As it is throughout the TPC Network.



The goal at the TPC at Piper Glen in Charlotte, NC and all TPCs is to remain tournament-ready throughout the year.

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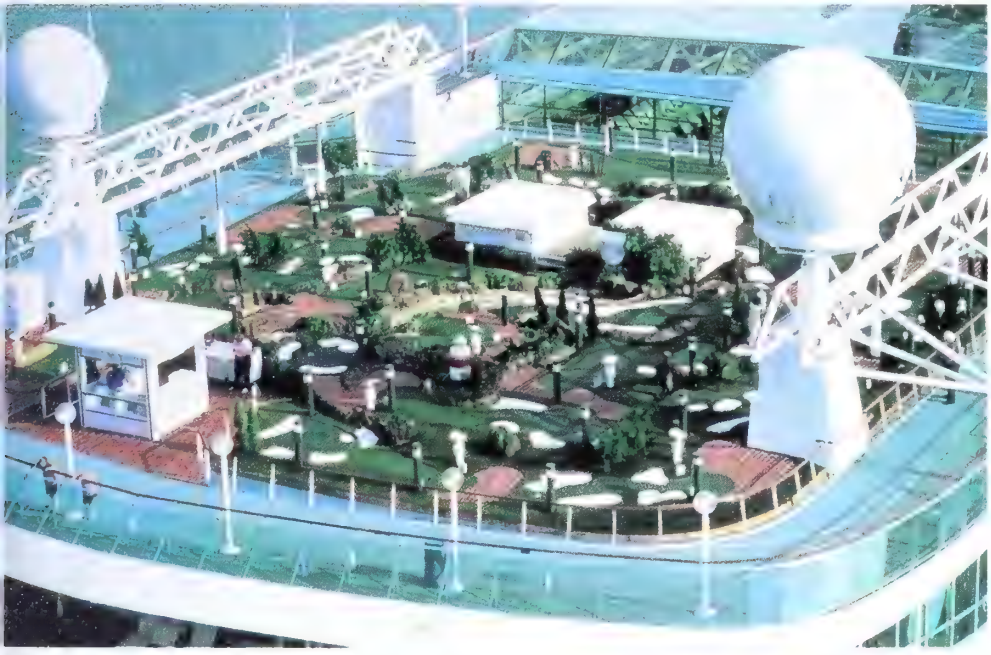
and Good Company

By Chelle Delaney

When it comes to golf, being 50-something isn't a bad deal. The players on the Senior PGA TOUR, who must be 50 to qualify, prove it. Some of them are earning more on the Senior TOUR than they did on the PGA TOUR.

The Senior TOUR itself is doing well.

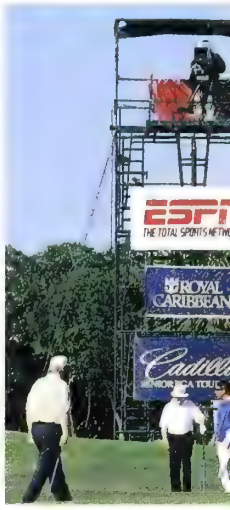
From two events and prize money of $250,000 back in 1980, the Senior TOUR in 1996 has developed into 44 events and more than $37 million in prize money.



Royal Caribbean reaches the audience it wants most effectively through its association with the Senior PGA TOUR.

Another winner: Charity.

As the Senior TOUR has grown, so has its contributions to charity. Just one tournament, the Royal Caribbean Classic, which contributes to Miami charities, is expected to reach the $1 million mark this year. "That's our goal," says Mark Kammerer, director of marketing for Royal Caribbean, "so it's been a major win for the Senior TOUR."



STAN BADZ - PGA TOUR

And for Miami-based Royal Caribbean Cruises Ltd., the Senior TOUR and Royal Caribbean associate well. "The TOUR is mostly associated with beautiful places and warm climates, something that Royal Caribbean offers, as well," Kammerer says.

"But we need to do more beyond the single week of the tournament. We've been reviewing marketing ideas with the Senior TOUR, talking about the areas we want to cover, such as ways to reward the volunteers who are so vital to every tournament."

The Senior TOUR provides its marketing partners with in-depth marketing assistance. Leo P. McCullagh Jr., Vice President of Marketing and Retail Licensing, says, "We recognize the realities of the '90s; sponsors want to know how they can increase their return on investment. We've created three tiers of marketing service: from those on the executive level to the grass roots support staff at the tournaments. The three-tier integrated approach allows us to learn more about our client's business, figure out ways to make golf increase their sales and execute the promotions on site and at retail."

McCullagh adds, "We always hope our clients use their official status with the TOUR in their advertising and promotion. O'Doul's is a good example of a fully integrated corporate marketing campaign.

"They have golf theme ads, golf theme packaging and golf theme promotions at the point of sale. And they sample on-course at various golf tournaments."

Bill Ellis, the Anheuser-Busch brand manager for O'Doul's, says, "The majority of beer drinkers who have not tried a non-alcoholic malt beverage before have bad

product perceptions. Sampling has been very successful and is the best way to dispel those perceptions."

Sampling on the Senior TOUR is provided by an O'Doul's "Oasis" truck and sometimes via a golf cart with a half barrel of O'Doul's draft.

"Golf enthusiasts and the brand demographics match up very nicely," Ellis says. The association with golf also is used at the point of sale. For example, O'Doul's packaging incorporates the PGA TOUR logo.

This year, from April through June, every 12-ounce 12-pack will have an O'Doul's scratch golf game promotion card and consumers will have an opportunity to be instant winners. "We have over 20,000 prizes that we're incorporating into the promotion, tie-ins with golf equipment and grand prize winners for two to a PGA TOUR event. There's also an O'Doul's second chance sweepstakes that includes golf trips."

Another advantage to being a Senior TOUR sponsor is the Senior TOUR's marketing people.

O'Doul's Ellis says, "My experience with the people of the PGA TOUR is that they truly are our partners and truly interested in how they can maximize their return on investment through golf for their sponsors. They look for ways to enhance our ideas; they bring ideas to us that might help us meet our goals."

Lee Pinkard, national director of marketing and communications for Coopers & Lybrand L.L.P., New York, a professional services firm, agrees. "We're in constant dialogue with them. 'These are our goals. Here's the message. How can we deliver it?'"

"Our goals link with golf in two ways. We can reach a higher percentage of our total audience in golf than in any other way. And golf has the connotations of sportsmanship, fair play and high quality. Golf is a metaphor to talk about our people, who can help provide solutions."

There's another Senior TOUR sponsor in the relationship business Merrill Lynch & Co., Inc., New York, the nation's largest stock brokerage firm.

The Merrill Lynch Shoot-Outs, a 10-man, nine-hole elimination competition, are scheduled at 16 Senior TOUR events and 18 PGA TOUR events in 1996. The weekly $15,100 purse culminates in a $500,000 purse for the Merrill Lynch Senior TOUR Shoot-Out Championship, to be held at The Homestead in Hot Springs, VA.

"The Shoot-Outs are fun," says Claudia J. Kahn, first vice president, executive communications and client services, Merrill Lynch & Co. "They're popular with the players and the spectators."

On-course sampling at Senior TOUR events has been very successful for O'Doul's.

The Shoot-Outs, which have been played for about decade, typically are held on the Tuesday of a tournament week, so they add another day to the tournament and infuse additional money into the community.

Merrill Lynch Shoot-Outs are popular with the players and spectators.

"Merrill Lynch uses each Shoot-Out," says Kahn, "to entertain about 250 clients and prospective clients of our local or regional office. Prior to the Shoot-Out, we usually invite our clients to a business seminar and luncheon, where there is always valuable information to be shared along with the opportunity to have some fun. No where

Bayer is considering incorporating the Senior TOUR logo on some of its packaging.

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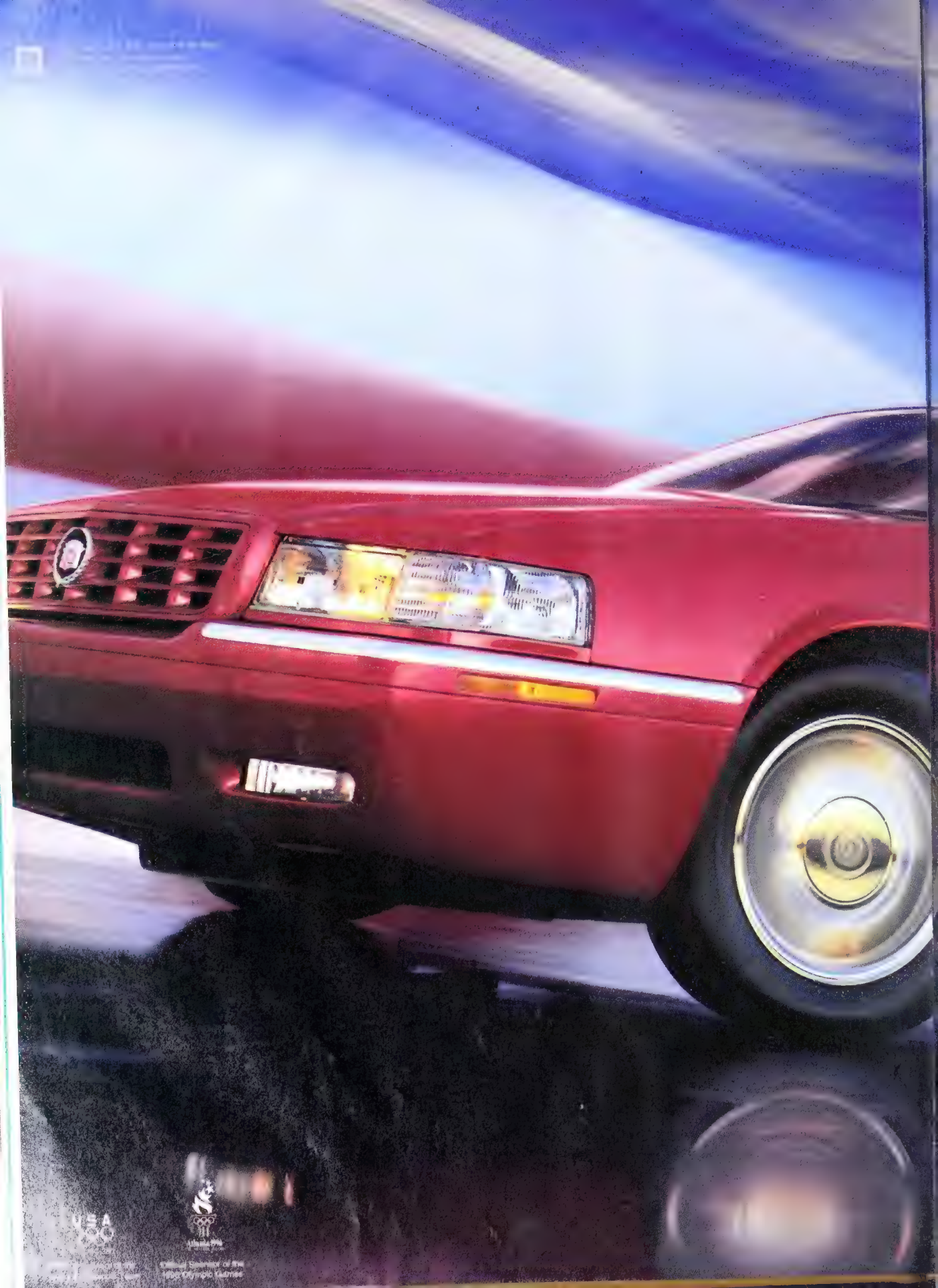

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And that brings up Team Bayer. In 1996, three PGA TOUR players and four Senior TOUR players (Tom Weiskopf, Dick Rhyan, Lee Elder and Dave Stockton) will boost the Bayer Corporation's program, "Strokes Against Stroke."

Each player has had some association with stroke or cardiovascular disease through their own personal experience, or that of a family member or friend.

So it means a lot to them that, during the month of May, which is "Stroke Awareness Month," Bayer will contribute $500 to the American Heart Association for every birdie recorded by every member of the team.

"In 1995, those $500 contributions added up to $50,000," says Jay Kolpon, Bayer marketing director, "and we hope that it increases this year. 'Strokes Against Stroke' is a win-win situation.

"That's why we've expanded our team for 1996. The American Heart Association gets money for stroke research and education, and Bayer and the Senior TOUR get terrific public exposure – which builds public awareness of the dangers of stroke."

PGA TOUR ARCHIVES

Coopers & Lybrand gets prominent display on electronic scoreboards at Senior TOUR events.

Bayer leverages its participation on the Senior TOUR with its televised Bayer Power Play and by entertaining customers, executives from drug and grocery chains and mass merchandisers. Kolpon adds, "it is a fully integrated relationship that really works for us."

The audience at Senior TOUR events is also ideally suited to *Business Week* magazine. Harold K. Somerdyk, vice president of marketing at Business Week, says, "The management audience is what *Business Week* caters to, and golf is certainly part of the landscape. That has led us to become the presenting sponsor of a brand-new, sanctioned event on the Senior TOUR that will be rather unique."

The American Express Invitational Presented by *Business Week* in Sarasota, FL, at the TPC at Prestancia, is scheduled the week of Feb. 19-25. That happens to coincide with the start of spring training for America's other favorite sport, baseball. The event will combine the legendary heroes of baseball with the legendary heroes of golf.

"Baseball," Somerdyk says, "is America's pastime, golf is America's passion."

Jack Birch, group director of Advantage International, a sports and event marketing company, is helping to organize and present the event. "It'll be awesome," Birch says. "Imagine Lee Trevino chasing down some famous baseball player for his autograph. Or vice versa."

This year, the Cadillac Series will include Royal Caribbean Cruise Lines. They have teamed up with Cadillac to sponsor ESPN television coverage of 20 Senior TOUR events in 1996.

Gust Kouvaris, account supervisor for Cadillac golf programs at DMB&B advertising agency, says, "The bottom line is that Cadillac didn't just buy blanket TV. We've got local involvement for our dealers, and we're associated with professional golfers. Fans see Cadillacs driving around. They see pros wearing the crest, meet them at local hospitality tents. They watch the game recap on TV and hear it referred to as part of the Cadillac Series. It's a great way for a great company to show off a great product and it sells cars."

Cadillac also offers opportunities to raise money for local charities. "Some areas have one-day events with amateur golfers and golf clinics to benefit charities like Multiple Sclerosis and Cystic Fibrosis," says Kouvaris. "The big one is the Cadillac Invitational for the National Kidney Foundation. There are 125 one-day tournaments, and Cadillac is the title sponsor of all of them. Fred Couples and Lee Trevino were the spokespersons for the Cadillac Invitational last year. It raised more than $3 million."

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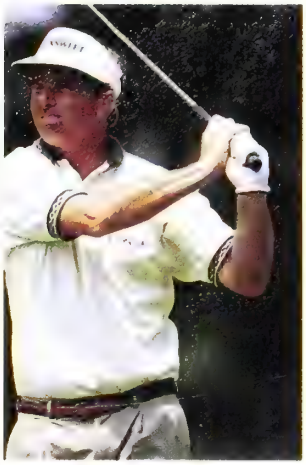
What's in the Bag

By Reid Hanley



You can find metal woods and a long putter in Gary Groh's bag.

Gary Groh is a very traditional guy. He doesn't even wear striped shirts.

You always knew what was in his golf bag. There would be two big persimmon woods, 12 forged Wilson irons and a conventional putter. In the ball pocket, you'd find real balata golf balls.

Things have changed. Groh, a Senior PGA TOUR rookie last year who is also head pro at suburban Chicago's prestigious Bob O'Link Golf Club, has been caught up in the wave of technology that is sweeping the Senior TOUR. Groh now has metal woods and a long putter. He likely will start the 1996 season with Wilson RM cavity-back irons. He might be using a blended covered golf ball, too. Titleist isn't making his beloved 384-Tour ball anymore.

Technology is limited only by the Rules of Golf.

"I'm the last guy to change," said Groh, who won the 1972 Buick Open and the 1975 Hawaiian Open. "Something I like, I stick with it. But when everybody else started using high tech stuff, I looked into it. Now they have so many different shafts and flex points. I tried a lot of them, and then I found one I liked and it really worked. I've stuck with it ever since."

The Senior TOUR is a working laboratory of golf technology. There are millions of dollars to be made out there, and the seniors are looking for any edge they can find to get their share of the pot. Manufacturers, eager to increase sales, are working furiously to put the best equipment in their hands and then advertise it. Players also are taking advantage of some technology designed for the average player and then refining it.

Technology is helping these over-50s play some of the best golf of their careers in spite of their age. They are hitting the ball as long or longer than they ever did. They are hitting just as many greens as they did 20 years ago and are putting the ball closer to the hole. Technology is the Senior TOUR's Fountain of Youth.

Technology is limited only by the Rules of Golf. Balls, woods, irons, putters have improved. Nothing is sacred.

The 1995 Energizer SENIOR TOUR Championship at the Dunes Golf and Beach Club in Myrtle Beach is proof that the Senior TOUR has gone high tech. According to the Darrell Survey, which keeps track of equipment use on the PGA TOUR and Senior TOUR, only two of the 45 elite players at the tournament used steel shafts in their drivers. The only wood players used was the peg they teed their balls on.

Eleven players, including Lee Trevino (above) and Ray Floyd (right), played a no-cut, two-piece ball at the 1995 Energizer SENIOR TOUR Championship.

Cavity-back irons were an overwhelming choice of the SENIOR TOUR Championship players with just a handful of forged blades being used. Putters, long and short, also have a modern look to them. There were 11 players who

played a no-cut, two-piece ball, including Lee Trevino and Raymond Floyd.

"The Senior TOUR is all about extending careers," said Senior TOUR player Bob Murphy. "It's also about extending your capability to play well. It's adapting golf clubs so they fit the individual. People who want to play better golf should avail themselves of stuff that has already been tested. You can tell what works by what guys out here are using."

What does this mean to the average golfer? Can the 18-handicapper peer into the bags on the Senior TOUR and learn from it? Using this information intelligently, you bet.

SAM GREENWOOD PGA TOUR

The standard driver is inching toward 44 inches. Rocky Thompson leads the Senior PGA TOUR with a 57-inch driver.

Many club makers say the shaft is more important than the clubhead, and here the choices are overwhelming. There are approximately 200 different shafts available for woods and 150 for irons. Steel is yesterday's news. Graphite has become so versatile, it can virtually do whatever a player wants it to. It can be light, as heavy as steel, stiff, flexible, make you hit it high or low. Light is the new wave.

Can the 18-handicapper peer into the bags on the Senior TOUR and learn from it?

"I've been able to take two ounces out of the shaft and put it in the head, which gives me a bigger clubhead mass," said Trevino.

"When I connect with the ball, there is not as much recoil and you're going to get an extra five, six, seven yards."

The long putter is becoming less of a factor on the Senior TOUR. The hottest putters among the seniors are the Odyssey putters that feature a soft-faced insert. They add steel for players using a two-pieced ball.

You can buy the same clubs that the winners on the Senior TOUR use, but to take full advantage of the technology that wins millions, you need to get your clubs custom fitted like the pros do. That's not as hard as you might think. Twenty-seven manufacturers offer club fitting programs that will put the right set in your bag.

Go to a full service pro shop and get the sticks Trevino, Murphy, Groh and the rest of the Senior TOUR players use. Get them fitted properly, and then buy the same balls they use. Step up to the cash register.

The golf ball is most basic to the game, and some players have been slow to change. Trevino wasn't. Since changing to a solid two-piece ball, Trevino has won 27 tournaments and almost $5 million.

"Yeah, that ball's not too bad," said Trevino, who uses Spalding's Top Flight Z-Balata.

"Let me tell you something, for as much money as we play for out here, if I didn't think I could play with this ball, I wouldn't. It's too late in life."

The trend is to synthetics like surlyn, lithium balata, z-balata, zylin, iotek and blends. No cut balls can be tailored to every flight pattern and combine distance and durability.

Oversized woods and irons are a hit on the Senior TOUR. They think bigger is better because of the expanded sweetspot's accuracy. Clubs are getting even bigger than oversized, like the increasingly popular Callaway Great Big Bertha that leading money winner Jim Colbert uses. They could become the norm.

SAM GREENWOOD PGA TOUR

Jim Colbert favors the Callaway Great Big Bertha.

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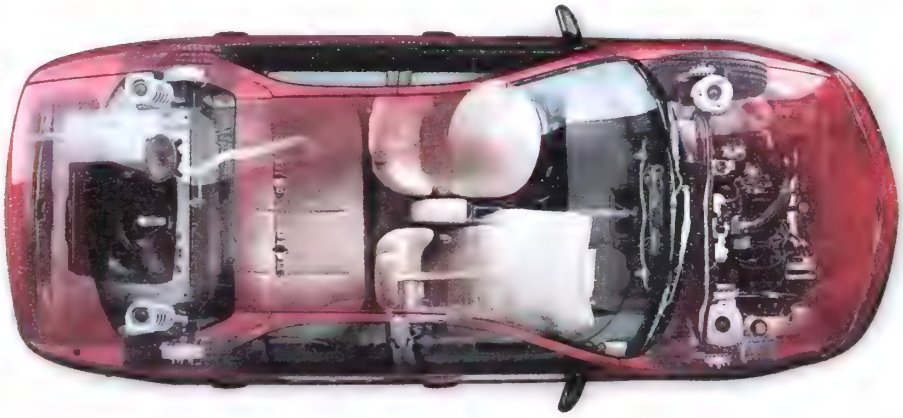

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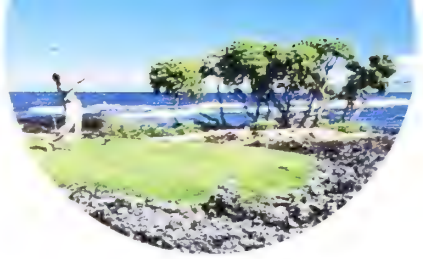

Hualalai: A Course Set in Stone

By Chris Smith

The MasterCard Championship, formerly the Senior Tournament of Champions, assumes a dramatic new look in January 1997, one that literally can be found only in the middle of the Pacific Ocean.

Senior PGA TOUR winners from the 1996 season will discover a tropical arena of startling contrasts, of imposing dark rock, rich green fairways and inviting turquoise waters. It is a setting that is both stark and unusually beautiful, created by the most volatile of nature's elements and most imaginative human minds.

The location is the Big Island of Hawaii, specifically the western extreme known as the North Kona Coast.

The venue is the new oceanside residential resort Hualalai, reverently named after the true architect of this memorable landscape, a dormant volcano that rises majestically some 10 miles inland.

Featuring a Four Seasons Hotel that is scheduled to open in the fall of '96 and designated a PGA TOUR Resort, Hualalai is an oasis of elegance, charm and beauty, having evolved through the marvels of creative vision and modern machinery.

The last of its namesake's eruptions poured molten lava toward the sea nearly 200 years ago. It is within this tangle of rock that the course has been chiseled and blasted to the specifications of Jack Nicklaus. Roughly 120 acres of brilliantly green turf are set within the foreboding blacks, grays and browns of the lava.

"Every time I came, we kept widening this place," Nicklaus recalled. "You want to keep the lava just out of play, but in play visually. It can be a great feature visually, but it also can be a pretty stiff hazard. I don't care how far back you crush the lava, though, people are going to get into it."

Offering the variety of five sets of tees ranging from 5,282 yards to 7,094, the course flows naturally with the terrain, a gentle five-degree slope toward the sea from the base of the volcano. Each hole has a view of the Pacific, though the finish is particularly dramatic. Nos. 15 and 16 play toward the ocean, the par-3 No. 17 cuts along the coastline and the 18th tee is nestled on a peninsula of lava.

Throughout the course, lava establishes the absolute boundaries of each hole, at times with actual walls of rock.

"One of the nice features of a lava course," Nicklaus said, "is that while most courses have to be planted out when they are done, a lava course is framed from Day One."

But to create the picture within that frame is a laborious task of crunching, blasting and heavy machinery.

There is no subtle way to shape a course in solid rock. Once Nicklaus established the routing and elevation specifications of each hole, the heavy equipment arrived to begin crushing and scraping lava. Everything from the fairways and bunkers to the irrigation system literally had to be cut from rock. What the big machinery couldn't handle was blasted.

"Lava creates a different situation," Nicklaus said. "You have to crush it, then put down the top soil. But all the form must be in the crushed lava."

The entire course ultimately was set in stone before a choker layer of several inches was spread to keep the final topsoil from falling through the cracks. Finally, more than 300,000 cubic yards of dirt were spread over the growing area. Once completed, the actual growing of the course was easy.

"I'm really pleased with the final product," Nicklaus said. "This project took some time, and I think those who play it will see the efforts that went into it."

And now it prepares to showcase the best players on the Senior TOUR, a course as unique as the setting itself.

"I certainly am eager to see the Senior TOUR go there," Nicklaus added. "Of course, when you have your name on a golf course, you are a little nervous, too. I think the guys will like what we have done. Plus, it is such a beautiful setting. That's what I like most about projects in Hawaii. You are able to have a wonderful, natural setting on each hole.

"I'm pretty confident the layout will provide a good combination – it's challenging and fair."

With ocean on one side, volcano to the other and expanses of hardened lava, Hualalai makes for dramatic and visually intimidating golf.

Photography by John Severson

Tips from the Senior TOUR

By Phil Stambaugh with Jim Colbert

Save Strokes By Crossing the Hands Over

Golfing legend Bobby Jones once said that the secret to shooting low scores is the ability to turn three shots into two. The higher your score, the faster you can lower it – with the short game.

Since joining the Senior PGA TOUR in 1991, Jim Colbert has had one of the best short games on the circuit. That was never more evident than during the season-ending Energizer SENIOR TOUR Championship last November in Myrtle Beach, SC.

His deft touch with a variety of clubs from around the small, undulating greens at The Dunes Golf Club contributed heavily to a wire-to-wire victory and $262,000 first-place check – the largest in Senior TOUR history. The win was Colbert's fourth in 1995 and not only propelled him to his first Arnold Palmer Award as the circuit's leading money-winner, but also to his first Player of the Year honor from a vote of his peers.

"I really don't think many professionals and good amateur players understand the fundamentals of a good short game," Colbert says. "The short game is really just an extension of the overall golf swing. The key is to get yourself in the strongest position you can to hit the ball. Once in a powerful position, I can control the clubhead and hit a shot as hard or as easy as I like. In order to do that, the arms should stay close to the body, the left side should clear out of the way and, most importantly, the right hand should ALWAYS be allowed to cross over the left through the shot, whether you're talking about a full shot, a pitch shot, a chip shot or a bunker shot."

Remember, any shot in Colbert's short game and that of most touring pros is a RIGHT-handed, RIGHT-sided shot. Imagine any shot from around the green as just a mini-golf shot, and make sure to allow the RIGHT HAND TO CROSS OVER THE LEFT. The handle of the club never should go toward the target. The clubface goes toward the target!

After mastering the proper technique, Colbert believes it's easy to adapt to any situation a player faces around the green.

A slight change in posture is all that is needed when attempting to hit pitch and chip shots high or low. For higher, softer shots, stand up straighter at address. The more one bends the trunk of the body, the lower the trajectory of his shot.

In order to get the ball close to the hole, Colbert emphasizes the importance of simplicity when measuring distance.

"I generally try to judge everything from point 'A' to point 'B' or from where my ball is to where the hole is located," he says. "If I think about trying to land the ball on a particular spot, then I've got an 'A', a 'B' and now a 'C' to think about."

The bottom line is that the RIGHT hand should always cross over the left.

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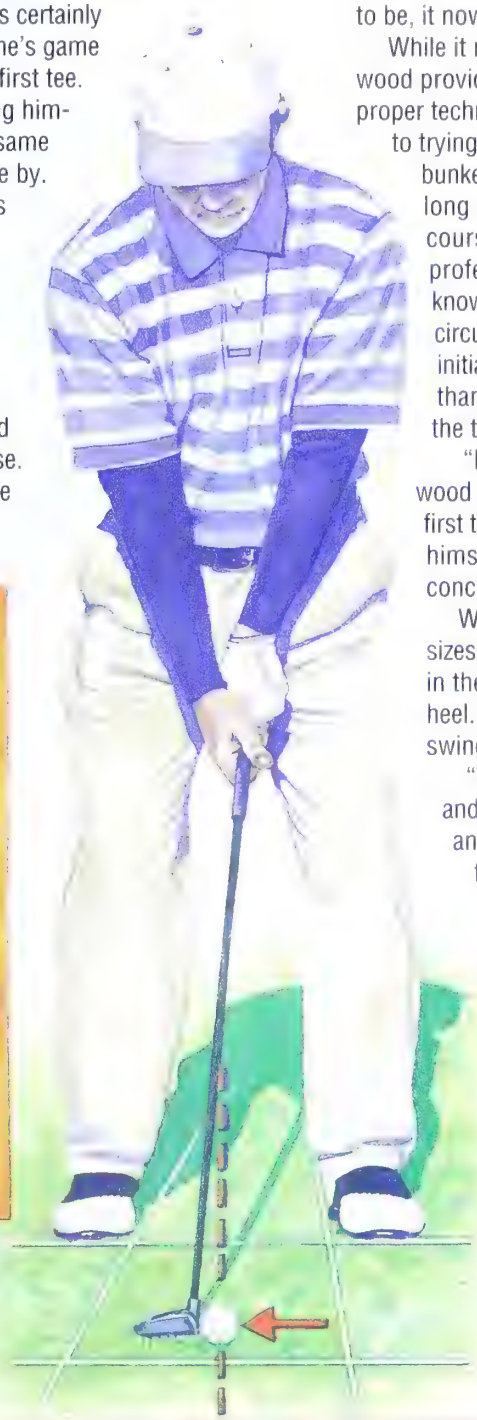
Tips from the Senior TOUR

By Phil Stambaugh with Bruce Summerhays

Utility Woods Might Save Your Game

Long irons. Most average players struggle to hit them consistently, and have even greater trouble convincing themselves to seek an alternative as they get older. Clint Eastwood's famous movie line about a man knowing his limitations is certainly true when it comes to taking one's game from the practice range to the first tee. A senior citizen could be fooling himself if he thinks he can hit the same shots he executed in days gone by.

As a player gradually moves into his fifties on the golf course, his body might have trouble keeping up with what his mind tells him to do. Unless he's Jack Nicklaus or Tom Weiskopf, he probably should check his long irons and ego at the door of the clubhouse. It's time to move on and put the utility woods in the bag.



At one point in his career, a player might have been able to hit a high shot and get the ball to land softly on the green from 195 yards with a 3-iron. But because he isn't aware – or won't admit – his muscles aren't as supple as they used to be, it now might take a 5- or 7-wood to get the job done.

While it might lack the sex appeal of a 1-iron, the utility wood provides some functionality and is easy to hit if the proper technique is used. The club is also a great alternative to trying to play a shot from heavy rough, a nasty fairway bunker or an unforgiving hardpan with a shallow-faced long iron that has little margin for error. Over the course of his rookie season last year, former club professional Bruce Summerhays gradually became known as one of the best 5- and 7-wood players on the circuit. By using these clubs effectively, he finished his initial campaign on the Senior PGA TOUR with more than $700,000 in official earnings and was among the top 10 in over one-third of his appearances.

"Most amateurs think *power* when they get a wood in their hand," Summerhays says. "Mentally, the first thing an average amateur needs to do is convince himself to let the loft of the club do the work and concentrate on just swinging smoothly."

When using a utility club, Summerhays also emphasizes the importance of ball position – situating the ball in the middle of the stance rather than near the left heel. The desired path of the club is a steeper downswing and a more descending blow into the ball.

"With the ball located too far forward in the stance and opposite the left heel, a player will swing upward and try to help the ball into the air. It is impossible for him to consistently use the loft of the club properly," he explains. "Basically, the player should have the same thought process that he does with a short iron in his hand: play the ball toward the *middle* of his stance and come into it with a sharp downward angle, even to the point of actually taking a divot," Summerhays says.

Trying a utility club in place of those hard-to-hit long irons might be just what the doctor ordered for many frustrated players. Combine that with a different ball position and some practice, and one is sure to see positive results.

ILLUSTRATION: IRENA ROMAN

Other Luxury Sedans Negotia
This One Seizes It

The Road.

V-8 Powered Lincoln Continental With Road-Calibrated Suspension

Throw a twisty mountain road or a teeth-rattling stretch of potholes at a lot of luxury sedans and they just passively accept the situation. Present the same to a Lincoln Continental, however, and it rolls up its sleeves and goes to work.

Sensors in Continental's exclusive Road-Calibrated Suspension "read" the driving conditions, then relay that information to powerful microprocessors. They, in turn, change Continental's shock-absorber damping between normal and firm to provide better handling to match the situation. It all happens faster than the blink of an eye.

The Road-Calibrated Suspension is a perfect complement to Continental's InTech™ System, a technological showcase that includes a responsive 32-valve, 260-horsepower V-8 engine.

But even though Continental exhibits an almost sports-car-like approach to the road, it is still first and foremost a luxury car. Its spacious cabin is trimmed in hand-finished walnut. The supple leather of its seats was selected not just for its look and feel but also for its scent. And at every corner there are impressive features like dramatic virtual image instrumentation and a 12-function Memory Profile System.

So instead of just negotiating the road, why not take control of it? In a Lincoln Continental. To learn more, call 1 800 446-8888 or, for information via the Internet, enter http://www.Lincolnvehicles.com.

LINCOLN

What A Luxury Car Should Be

You never practice. He never practices. You rarely play. He rarely plays. He's won 13 PGA events. You barely break 90. What gives?

Life is full of irony – especially if you golf. Consider Bruce Lietzke. After 21 years as a pro, you'd expect him to slow down and start scoring somewhere in your neck of the woods.

Well, he did slow down. But despite his relaxed pace, Bruce continues to score low enough to make younger pros shred their scorecards in envy.

"What's the deal?" you may ask. After all, he probably practices less than you do. And he plays just a few events each year in order to spend more time with his family.

Without taking anything away from Bruce's talent, we suggest that the right clubs can help. Like the oversize 855s Golden Scot Irons and Metal Woods from Tommy Armour. With a progressive offset and increased sole width, they're more forgiving than other clubs. And the oversize sweet spot and lighter graphite shaft will help you achieve maximum distance, even though your backswing may be a little shorter.

At Tommy Armour, we believe experience – and the right clubs – truly can lead to better scores. And that's what golf is really about – improving your score.

So even if you don't have Bruce's skills, you can still play better golf. Just pick up a set of Golden Scots. After all, if he isn't spending every available moment on the driving range, why should you?

For more information, call 1-800-468-7268 or visit our World Wide Web site at http://www.tommyarmour.com.

Oversize Golden Scot 855s Irons & Woods

Tommy Armour

TAKE YOUR GAME TO THE NEXT LEVEL

GULATORS

OW DO YOU POLICE YBERSPACE?

e FTC's Varney wants Net folk to help write the rulebook

o the dismay of seasoned net surfers, government arrived in free-wheeling cyberspace last year with a heavy hand. Congress proposed il anyone sending smut online. A al judge ruled against Prodigy Ser- Inc. for libel. And abroad, Ger- authorities barred CompuServe Inc. offering sites containing pornog-y. Internet pioneers were outraged e intrusions.

ut as cyberspace increasingly be-es a medium of social transaction commerce, government efforts to late it are sure to increase. Enter stine A. Varney, 40, the youngest ber of the Federal Trade Com-ion. Her mission: To become the U. S. Cyber-Marshall, protecting consumers buying products and services online against fraud, deceptive ads, and privacy violations. "The laws on the books should exist in cyberspace, too," she says.

Varney, a Clinton appointee who joined the FTC in October, 1994, insists she isn't about to strangle the burgeoning technology with rules. "As a New Democrat, I believe we don't know nearly enough to regulate now," she says. That's why she endorses industry self-policing as a first step. In September, she inaugurated the FTC's Privacy Initiative, inviting consumers, online service companies, advertisers, and others to propose voluntary industry guidelines to protect the privacy of Internet users by spring. To get the dialogue going, the FTC has established a Web site, which has logged almost 200 comments so far.

BRAVE NET WORLD: Varney believes that "the laws on the books should exist in cyberspace, too"

Cyber-snooping is not big business yet. But with electronic marketing expected to take off this year, Varney is heeding predictions that consumers will clamor for more safeguards against marketers culling personal data from their virtual communications. In the meantime, the former partner at the Washington law firm of Hogan & Hartson has spurred FTC probes into alleged fraud and misleading advertising in cyberspace. Several cases—including actions against advertising in the guise of anonymous online testimonials—will be unveiled this spring.

Varney is no stranger to the Brave Net World. As former Cabinet Secretary for the Clinton White House, her job was to monitor and coordinate communications among the Administration's agency chiefs. But the longtime cybersurfer was shocked that her wards didn't have E-mail and pushed to get them wired.

UNLIKELY ALLIES. Now her go-slow attitude on regulation worries privacy rights advocates. The FTC has "adopted a see-no-evil, hear-no-evil strategy," complains Mark Rotenberg, director of the Electronic Privacy Information Center. "Because the FTC is not prepared to protect privacy, there will be tremendous waffling" in the industry.

But Varney has support from some unlikely allies, who share her fear that tight regulation of the Net may be premature. "You don't want to regulate this new frontier to death before giving it a chance to live and flourish," says Richard F. O'Donnell, spokesman for the Progress & Freedom Foundation, a conservative think tank allied with House Speaker Newt Gingrich. And many in the Net *avant garde* agree. "We're in the age of the Stanley Steamer trying to figure out how I-95 is going

ARNEY'S AGENDA *Commissioner Christine Varney will lead the Federal Trade Commission's search for ways to protect consumers from abuses in cyberspace.*

AUD Law-enforcement authorities tracking down fraudsters hawking eir wares online. In 1995, the FTC ed a credit repair shop, and state gulators pursued everything from ramid schemes to miracle cures.

MISLEADING ADVERTISEMENTS The FTC is investigating deceptive ads in cyberspace—such as product endorsements by company representatives offered anonymously in casual chat-room talk.

PRIVACY The FTC supports a self-policing mechanism against violations of customers' privacy. It wants consumers to decide whether information gleaned from their E-mail and Web visits is disclosed to marketers.

It prints. **It copies.**

(It does not, unfortunately, monitor taste.)

Introducing the first color printer-copier. The HP CopyJet

Look at the vivid color. Look at the flawless reproduction. Don't look at the hat. What's important is that the new CopyJet gives you the quality you'd expect from an HP color printer, and it has the full functionality of a color copier. Besides the departmental convenience, the CopyJet is easy to operate and uses pl paper. If the whole department needs co printing and copying, there's the netwo ready HP CopyJet M*, for $3199. That's js a fraction of the money you won't have spend for color copies. Which will make look good, no matter what you're wear

$2495*

*E [illegible] U.S. retail price. Actual price may vary. †With Adobe PostScript. Adobe PostScript is a trademark of Adobe Systems Incorporated. FE12584

HEWLET PACKA

to work in 50 years," says D.C. attorney Ronald Plesser.

While Varney believes the FTC can police online fraud and deceptive ads through traditional enforcement, she thinks protecting privacy will create the greatest challenge for regulators because fast-changing technology presents totally new ways for business to observe consumers' habits. For example, marketers may soon be able to track someone's "clickstream"—the areas in cyberspace that a consumer clicks on to with a mouse, including all Web sites visited, pages accessed, and time spent per page. That could provide a starkly revealing glimpse of an Internet user. Given such possibilities, "we do need to exercise some self-control," says Roland J. Sharette, vice-president at J. Walter Thompson USA in Detroit, which represents online advertisers including Ford Motor, Motorola, and Kodak.

For now, electronic privacy concerns center on the sale of E-mail addresses to marketers interested in sending solicitations via the Net. A handful of mailing-list brokers have recently launched E-mail businesses. Altoona (Pa.)-based net.net advertising inc., for example, is about to rent a list of 1 million E-mail addresses collected from the Net to four large corporations, including Shell Oil Co. Net.net is clipping the list into 100 interest categories—including sports, arts, and investments. But the company claims to protect privacy by allowing consumers to opt out of the mailing list—similar to a database maintained by the Direct Marketing Assn. that allows consumers to avoid receiving snail-mail solicitations.

PRIVACY EDGE. Cyber-marketers recognize that such protections might lure more consumers into electronic transactions—from shopping to banking. "If you don't respect privacy, the industry is not going to grow," says William J. Tobin, president of Oakton (Va.)-based PC Flowers & Gifts Inc., a pioneering online marketer. And guaranteeing privacy may give one online service provider an edge over others. "Consumers are starting to shop around," notes Bill Burrington, assistant general counsel at America Online Inc. in Vienna, Va.

Still, online service companies are unlikely to give up the revenues they're getting from selling information about their subscribers to marketers. AOL and CompuServe sell such data, and Prodigy will send messages to targeted subscribers on behalf of advertisers.

But the industry realizes it has to come up with its own rules of the road—at least to stave off burgeoning attempts by the states to regulate online privacy. The online service companies successfully scuttled a proposal introduced in Maryland last fall requiring them to give subscribers the opportunity at least every year to opt out of receiving unsolicited E-mail. Now, a Minnesota lawmaker is contemplating introducing a measure prohibiting online service providers from giving out personal information about their users without their consent.

> Marketers recognize that allowing users to opt out of E-mailing lists might lure more of them into electronic transactions—from shopping to banking

The industry has just begun to devise minimum privacy standards under the auspices of the Interactive Services Assn.—which may offer on-screen options for consumers to click on to bar the use of personal data. But some businesses balk at rules they say would put them at a disadvantage to other industries. For example, if E-mailing your personal shopper at Nordstrom's entails lots of time-consuming questions aimed at securing consumer consent on private information, you might simply use the telephone. "Erecting huge numbers of roadblocks becomes burdensome for E-mail-based transactions," says William R. Moroney, president of Multimedia Telecommunications Assn., which represents phone and computer technology companies.

An even greater challenge is the global nature of the technology. "We could run our company off a sailboat in the middle of the ocean," says Philip E. Devorris, net.net's president. "I don't know how you could police it."

Even Varney admits that her initial moves at cyber-regulation are just the beginning of a long process. "I don't think self-regulation ultimately will provide all the answers," she says, envisioning a time when the government may have to adopt more aggressive rules. "But it's a good start." Varney only hopes that in the end, both technology and consumers win.

By Catherine Yang in Washington

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Call now or contact us at http://www.hp.com/info/1133 and we will send you print samples demonstrating the incredible color reproduction of the HP CopyJet. We will also be glad to include a detailed product brief explaining our inkjet technology with precision digital color imaging. Find out about the HP CopyJet and start saving money on color printing and copying today. A year from now you'll be happy you did.

HEWLETT PACKARD

pecial Report

THE BEST MUTUAL FUNDS

ll you need to know to pick ıe ones that fit your needs

fter a year like 1995, who's going to complain? Diversified equity mutual funds, the meat and potatoes of most investors' portfolios, earned an average return of 32.1%, including dividends and capital gains. Think ur funds' managers are so smart? Think again. The Stanrd & Poor's 500-stock index recorded a smashing 37.5% re-n, and it beat more than 80% of the mutual-fund managers. ·en with its stock-picking smarts and trading prowess, the 3.7 billion Fidelity Magellan Fund came close but could not at the market.

Maybe you made a lot of money, but perhaps you could ve made more in another fund. Or perhaps you could have d a fund that earned as much without taking as much k. Last year, risk-taking paid off, but the returns earned in 95 were a once-in-two-decades occurrence. And investors ntinue to throw money at funds—an estimated record $16 lion in the first three weeks of 1996, says Robert Adler of G Data Services, which tracks flows to funds. But this ar, returns will likely be tempered and the market not so ·giving to those who misjudge their risks.

LONG VIEW. That's why you need the BUSINESS WEEK Mul Fund Scoreboard. It's a feast of information on 885 equity nds that's an indispensable tool for mutual-fund investors in nitoring the funds they own or searching for the funds ·y need to build their investment programs. Want some ggestions? We've asked four investment advisers who spelize in mutual funds to design portfolios that fit the kind of ancial goals you must meet (page 104).

The Scoreboard includes what you need to know about a nd's performance, fees, and expenses. We examine returns rned over the past three-, five-, and 10-year periods, both fore and after taxes. After all, it's not what you make but t you keep that counts. We peer inside the portfolio to see what's behind the numbers. We look at "turnover," or how frequently the fund trades, "style," the kinds of stocks it invests in, and its largest holding. We also categorize the fund's risk from "very high" down to "very low."

The Scoreboard takes risk seriously. It's what sets the BUSINESS WEEK ratings apart from most others. At BW, it's not enough to get the highest returns: A fund has to get the highest returns after adjusting for the risk its managers took with your money. And we don't award ratings to hot performers that burst on the scene in the past year or so. We rate a fund only after it has built a five-year track record, long enough to see how the fund performs in a variety of market conditions.

We know you've been taking on a lot more risk. During 1995, some 60% of the estimated $120 billion that poured into equity funds went to the riskiest categories of funds, such as growth, maximum growth, small-company, and specialty funds,

CHARD ASEBROOK
can make ore by select- g good stocks in by trying shift assets ound"

ARREN ABELLE
he bulk of our nd is small- p, but it's not r mandate. We where we can ake money"

The Top Performers

These equity mutual funds have earned three upward-pointing arrows in the BUSINESS WEEK Mutual Fund Scoreboard. To get this rating, they needed to deliver superior risk-adjusted total returns over the last five years.

FUND	AVERAGE ANNUA'L TOTAL RETURN*	INVESTMENT OBJECTIVE	RISK
ALLIANCE GROWTH B	23.8%	Growth	Average
BABSON ENTERPRISE	19.8	Small company	Low
BERWYN INCOME	16.1	Asset allocation	Very low
CRABBE HUSON EQUITY	20.6	Growth	Low
EXCELSIOR INCOME & GROWTH	17.7	Growth/income	Very low
FAM VALUE	18.8	Small company	Low
FIDELITY ADVISOR GROWTH OPPORTUN. A	22.4	Growth	Low
FIDELITY CONTRAFUND	24.1	Growth	Average
FIDELITY DESTINY I	23.7	Growth	Low
FIDELITY DESTINY II	24.1	Growth	Average
FIDELITY EQUITY-INCOME II	22.0	Equity-income	Low
FIDELITY GROWTH & INCOME	21.2	Growth/income	Low
FIDELITY LOW-PRICED STOCK	24.3	Small company	Low
FIDELITY SELECT HOME FINANCE	39.1	Financial	Average
FIDELITY SELECT REGIONAL BANKS	32.1	Financial	Average
FIDELITY VALUE	20.8	Growth	Low
FRANKLIN BALANCE SHEET INVESTMENT	22.3	Small company	Very low
FRANKLIN INCOME I	17.6	Balanced	Very low
HANCOCK REGIONAL BANK B	33.8	Financial	Low
HEARTLAND VALUE	27.8	Small company	Low
IDS DIVERSIFIED EQUITY-INCOME A	16.8	Equity-income	Very low
INCOME FUND OF AMERICA	14.7	Asset allocation	Very low
INVESCO STRATEGIC FINANCIAL SERVICES	28.0	Financial	Average
INVESCO TOTAL RETURN	15.3	Asset allocation	Very low
LIBERTY EQUITY-INCOME A	19.3	Equity-income	Very low
LINDNER DIVIDEND	15.8	Balanced	Very low
LONGLEAF PARTNERS	23.3	Growth	Low
MERGER	12.1	Growth	Very low
MERRILL LYNCH GLOBAL ALLOCATION B	15.2	Multi-asset global	Very low
MUTUAL BEACON	18.8	Growth/income	Very low
MUTUAL QUALIFIED	19.5	Growth/income	Very low
MUTUAL SHARES	19.1	Growth/income	Very low
OPPENHEIMER MAIN ST. INCOME & GROWTH A	30.6	Growth/income	Average
OPPENHEIMER QUEST OPPORTUNITY VALUE A	23.5	Asset allocation	Low
PIONEER CAPITAL GROWTH A	25.4	Small company	Low
PIONEER EQUITY-INCOME A	17.6	Equity-income	Very low
T. ROWE PRICE CAPITAL APPRECIATION	14.4	Growth/income	Very low
T. ROWE PRICE EQUITY-INCOME	18.0	Equity-income	Very low
T. ROWE PRICE SMALL-CAP VALUE	20.6	Small company	Very low
T. ROWE PRICE SPECTRUM INCOME	11.2	Asset allocation	Very low
SELIGMAN INCOME A	15.1	Asset allocation	Very low
SKYLINE SPECIAL EQUITIES	23.7	Small company	Average
SMITH BARNEY PREMIUM TOTAL RETURN B	15.1	Equity-income	Very low
SOGEN INTERNATIONAL	13.8	Multi-asset global	Very low
STEINROE CAPITAL OPPORTUNITIES	26.2	Maximum growth	Average
STRONG COMMON STOCK	25.6	Small company	Average
THIRD AVENUE VALUE	21.2	Growth	Low
WINTHROP FOCUS AGGRESSIVE GROWTH	21.0	Maximum growth	Low

*1991–95, pretax return, includes appreciation plus reinvestment of dividends and capital gains

DATA: MORNINGSTAR INC.

cording to Avi Nachmany of Strategic Insight, a mutual-id consulting firm. In 1994, the riskiest funds took just one-rd of the money, and in 1993, only one-quarter. The reasons the shift? Perhaps investors are lengthening their horizons, alizing that more short-term volatility could mean better g-term results. The other reason, says Nachmany, is sim-r: "Money flows to the best performers, and that's where the performance has been."

This year, 48 funds earned three upward-pointing arrows, the highest rating for the period 1991 through 1995 (table). The ratings and all Scoreboard data are prepared for BUSINESS WEEK by Morningstar Inc., the fund ratings company. The top-rated funds span the investment spectrum from the T. Rowe Price Spectrum Income Fund, an asset allocation fund with an 11.2%-a-year average annual return, to Fidelity Select Home Finance, a specialty fund concentrating on savings-and-loan stocks with a 39.1%-a-year average annual return. It's a varied lot; it includes eight funds specializing in small companies and two maximum-growth funds, those empowered to take the biggest risks. What they all have in common is that they give their shareholders the most reward for the amount of risk taken.

HAT TRICK. The list includes 17 holdovers from last year, and several have been on the list frequently in the past—including Heartland Value, Lindner Dividend, and SoGen International. It also includes repeaters such as Mutual Beacon, Mutual Qualified, and Mutual Shares, all run by the same portfolio manager, Michael F. Price. Price's fund are unique, investing in bankruptcies, corporate reorganizations, and private placements and mergers—and there is some question about their future. Last week, BUSINESS WEEK reported that Price is trying to sell the funds' management company to pursue investments on his own (BW—Jan. 29).

Price isn't the only mutual-fund manager to pull off a hat trick. Fidelity's George A. Vanderheiden has three funds with three up-arrows, all for the first time: Fidelity Advisor Growth Opportunities A, Fidelity Destiny I, and Fidelity Destiny II. Tapping Vanderheiden's expertise isn't cheap—the two Destiny funds carry stiff 8.24% loads, among the highest of all funds in the Scoreboard—and that's not all. The two funds are sold as installment plans, which obligate investors to make monthly payments of $50 to $10,000 for a 10- or 15-year period. The cost for dropping out early can be stiff. In the first year, half the monthly investment goes to paying a sales charge. Vanderheiden's Advisor fund, a part of the Fidelity family that's sold by brokers and financial planners, carries a 3.5% load.

If you're worried about the high level of the stock market

and the high prices of many stocks, you will like the three-up-arrow funds. All have average or less-than-average risk profiles. Of them, 36 practice a "value" investment style: They buy stocks with below-average price-to-earnings and price-to-book ratios, as opposed to "growth" stocks, which have higher growth rates but higher p-e and p-b ratios. John Rekenthaler, publisher of *Morningstar Mutual Funds*, thinks the value-dominated list is particularly well-timed. "After last year's strong performance from the growth side," he says, "this could be the year for value stocks." Eleven funds are blends of value and growth, and only one, SteinRoe Capital Opportunities Fund, has a pure growth portfolio. The fund caught the crest of the growth-stock wave in 1995, racking up a 50.8% return.

Although she works in a highflying sector of the market, Gloria J. Santella, SteinRoe Cap's portfolio manager, strives to keep risk under control. She put a lid on technology stocks when they hit 25% of the portfolio, while many of her competitors increased their allocations to technology. "That hurt us early in the year, when tech did so well, but it certainly paid off in the fourth quarter," she says. She maintains a fairly concentrated portfolio, just 48 stocks, but argues that with fewer companies, she can minimize risk by doing more thorough research on each. Once she finds an investment she likes, Santella gives it time. Her portfolio turnover is only about a third that of her peer group.

GLORIA SANTELLA *She put a lid on technology holdings when they hit 25% of the portfolio*

Another new name on the top performers' list is Oppenheimer Quest Opportunity Value Fund A, managed by Richard J. Glasebrook. Categorized as an asset allocation fund, the portfolio's asset mix—87% stocks, 12% cash, and no bonds—looks more like that of a growth fund. "I can make more money by selecting stocks than by trying to shift assets around to take advantage of small moves in the capital markets," he says. "But I have the flexibility to preserve capital in a difficult market."

Glasebrook also invests in relatively small numbers of stocks, usually less than 50—"stocks everybody has heard of." Two of his largest positions are McDonnell Douglas Corp., a stock that doubled in price over the past year and now makes up 7.5% of the fund. The next-largest position is Intel Corp., about 5%. With a contrarian bent, Glasebrook was busy adding to his Intel stake on Jan. 18 when a bad fourth-quarter profit report triggered a glut of sell orders. "Intel's aftertax return on capital is over 20%," he says. "And its competition is falling further and further behind."

STRONG IN A REBOUND? The willingness to swim upstream is a key factor behind the success of Pioneer Capital Growth Fund A. Portfolio Manager Warren J. Isabelle hunts for Wall Street's unloved or unnoticed companies and selects those where he finds the most value. And he has so far been able to knock out double-digit returns every one of the past five years—including the very difficult 1994, when the average fund lost more.

Now, Isabelle's largest holding is the unloved Toys "R" Us Inc. In a small-company fund? "The bulk of our fund is small-cap, but it's not our mandate," says Isabelle. "We go where we can make money." Isabelle says Toys needs to revamp its format to put more emphasis on electronics, but its basic problem is the retail sales slump. "But it's a survivor," he says, "and in a rebound, it will have an operating and pricing leverage."

What's also notable about the top-performers' list is what it doesn't have—technology funds and international funds. Eight tech funds made the list for the 1990-95 period, but all slipped off in 1995, despite the 44.5% av

The Largest Funds

Here's how the BUSINESS WEEK Mutual Fund Scoreboard rates the largest equity funds

FUND	ASSETS BILLIONS	BW RATING	AVG. AN'L TOTAL RET.*
FIDELITY MAGELLAN	$53.7	▲	20.4%
INVESTMENT COMPANY OF AMERICA	25.7	AVG	14.6
WASHINGTON MUTUAL INVESTORS	18.8	▲	16.7
VANGUARD INDEX 500	17.4	▲	16.4
FIDELITY PURITAN	15.6	▲▲	16.6
FIDELITY CONTRAFUND	14.8	▲▲▲	24.1
FIDELITY GROWTH & INCOME	14.8	▲▲▲	21.2
TWENTIETH CENTURY ULTRA INV.	14.6	▼▼	25.0
INCOME FUND OF AMERICA	13.8	▲▲▲	14.7
VANGUARD/WINDSOR	13.6	▲	18.4
VANGUARD/WELLINGTON	12.7	▲▲	14.9
JANUS	12.5	▲	16.7
FIDELITY EQUITY-INCOME II	12.0	▲▲▲	22.0
FIDELITY ASSET MANAGER	11.2	▲▲	13.7
VANGUARD WINDSOR II	11.0	▲	17.6
FIDELITY ADVISOR GR. OPPORT. A	10.9	▲▲▲	22.4
EUROPACIFIC GROWTH	10.9	▼	13.4
FIDELITY EQUITY-INCOME	10.5	▲▲	18.9
DEAN WITTER DIVIDEND GROWTH	9.4	▲	15.6
NEW PERSPECTIVE	9.3	▼	15.0

*1991-95, pretax return, includes appreciation plus reinvestment of dividends and capital gains
LEGEND: (3 arrows up) superior, (2 arrows up) very good, (1 arrow up) above average, (1 arrow down) below average, (2 arrows down) poor, (3 arrows down) very poor

DATA: MORNINGSTAR INC

return from the tech funds. The funds plunged in the fourth quarter—along with the rest of the tech sector—and that lowered their risk-adjusted scores enough to cost them their top-notch ratings. The tech blow-off also took a toll on the Fidelity fund complex, which had taken big stakes in the sector and started to sell them off in the latter part of the year. In the first nine months of 1995, 13 of the 22 Fidelity growth-oriented funds in the Scoreboard beat the S&P; by year-end, only five were ahead of the index.

No portfolio of funds is complete without a dollop of international funds. But the best rating you'll find on a non-U.S. fund is average, and most are below average. That's because foreign markets have woefully underperformed the U.S. in four of the past five years. From 1991 through 1995, international funds lagged U.S. funds by nearly seven percentage points. In 1995, the gap was even wider, nearly 23 percentage points. Yet there's virtually no difference between U.S. and international funds over the past 35 years, says fund expert A. Michael Lipper of Lipper Analytical Services Corp. That leads him to believe non-U.S.

ow rate them a buy

funds are a buy. "The gap will close," he says, "if not in 1996, then in 1997." Indeed, some investors are already moving their money abroad. AMG's Adler says about 20% of this year's fund cash flow is going into non-U.S. funds.

In BW's Scoreboard, the best-rated international funds are "world" funds, but those funds combine both U.S. and non-U.S. stocks. They owe their stronger performances to the U.S. portions of their portfolios. To really play the rebound, select from the foreign funds, which explicitly don't contain any U.S. stocks. Among the better-rated foreign funds are GAM International, Managers International Equity, and the Templeton Foreign Funds. Lipper thinks the biggest rebounds will come in the battered emerging markets funds, particularly those investing in Latin America.

As you turn to the Scoreboard, note some of its features:

■ *Portfolio manager.* You'll see a head-and-shoulders figure next to some funds. If the figure is filled, the manager has been on the job 10 years or more—a plus in selecting a fund. If the figure is outlined, there's been a change in the past 12 months. Take note of Govett Smaller Companies Fund A, which got a new manager near the end of the year. That 51.1% average annual return for the last three years was someone else's work.

■ *Assets.* Rapid asset growth can cool a fund manager's hot hand. During 1994, Crabbe Huson Special Fund increased its asset base more than tenfold. In 1995, assets were up 143%—and the fund was up only 10.8%. (Part of the reason for the poor performance was that the fund sold tech stocks short well before they started to fall. That bet may yet pay off.)

■ *Expense ratios.* The average expense ratio for the Scoreboard funds is 1.28%. It hasn't gone up in the past few years, nor has it come down, which it should have, considering the funds have much larger asset bases over which to spread their cost. Note that some of the worst-performing funds have among the highest expense ratios.

■ *Pretax and aftertax returns.* Aftertax returns assume a 31% federal tax rate on income and short-term gains, and 28% on long-term capital gains. The difference between pretax and aftertax returns should be small for growth funds, but greater for yield-oriented funds such as balanced and equity-income funds. Yield-oriented funds may not be attractive for taxable accounts. But they make good choices for tax-deferred individual retirement accounts and 401(k) plans.

■ *Style.* You can't rely only on the name on the door, or the fund's investment objective to tell you how it invests. Despite its name, the Alger Small Capitalization Fund has a mid-cap portfolio, according to Morningstar's analysis.

Those are just some of the highlights. Plenty more await you, starting on page 110.

By Jeffrey M. Laderman in New York

The Fund Groups

The best stock market in two decades led to bountiful returns. Even though returns were high, the average fund could not keep up with the S&P 500. International funds were sluggish, and emerging markets funds were the only group to post a negative return for 1995.

FUND OBJECTIVE	AVERAGE ANNUAL TOTAL RETURN* 1995	1993–95	1991–95	1986–95	BEST PERFORMER IN 1995
HEALTH CARE	47.3%	15.7%	18.3%	19.6%	Dean Witter Health Sciences
FINANCIAL	45.7	18.0	29.5	16.4	Fidelity Select Home Finance
TECHNOLOGY	44.5	26.6	28.4	16.6	Fidelity Select Electronics
SPECIALTY	37.6	16.3	19.9	16.1	Fidelity Select Air Transport
MAXIMUM GROWTH	34.5	16.7	22.1	15.2	SteinRoe Cap. Opportunities
GROWTH	32.5	13.9	17.3	13.9	Wasatch Mid-Cap
SMALL COMPANY	32.2	15.7	21.5	14.4	Govett Smaller Companies A
GROWTH/INCOME	31.7	13.8	15.8	13.0	Washington Mutual Investors
EQUITY-INCOME	28.9	13.2	15.2	11.7	Vanguard Equity-Income
UTILITIES	28.1	10.3	12.0	11.8	Strong American Utilities
BALANCED	25.4	11.2	13.4	11.5	AIM Balanced A
NATURAL RESOURCES	23.7	14.2	10.3	9.2	Fidelity Sel. Energy Service
ASSET ALLOCATION	23.4	10.9	13.3	10.5	Oppenheimer Quest Opp. Val. A
COMMUNICATIONS	18.6	16.3	21.5	17.6	Flag Inv. Telephone Income A
MULTI-ASSET GLOBAL	18.5	10.8	11.1	11.3	Robertson Stephens Contrarian
EUROPE	18.0	15.9	10.3	9.4	Dean Witter European Growth
WORLD	15.3	13.7	12.3	12.1	AIM Global Agg. Growth A
REAL ESTATE	9.3	10.1	14.5	NA	Cohen & Steers Realty Shares
FOREIGN	7.9	14.1	10.9	12.6	GAM International A
PACIFIC	3.3	14.3	10.0	13.3	Colonial Newport Tiger T
PRECIOUS METALS	1.4	18.7	6.3	7.6	United Services World Gold
EMERGING MARKETS	–5.1	12.1	10.8	9.6	Vanguard Int. Eq. Emrg. Mkts.
U.S. DIVERSIFIED FUNDS	32.1	14.3	17.8	13.7	
ALL EQUITY FUNDS	26.9	14.2	16.3	13.3	
S&P 500	37.5	15.3	16.6	14.9	

*Pretax return, includes appreciation plus reinvestment of dividends and capital gains

DATA: MORNINGSTAR INC

Special Report

FOUR EXPERTS GO SHOPPING FOR YOU

To help guide the perplexed, here are model portfolios of funds for all sorts of investors

Browsing the vast range of mutual funds is like walking the supermarket aisles. Some of the items are fresh and tasty, some old and stale; some are bargains, some overpriced. And even if you select great food at good prices, your cart may not contain the right mix of ingredients to make a well-balanced meal.

That's why BUSINESS WEEK asked four expert "shoppers," investment advisers who pick mutual funds for their clients, to go shopping for you. We asked our experts to construct portfolios of funds that meet one of the kinds of investment challenges you may face, such as investing for a child's education or finding an optimal mix for your 401(k) plan. One pro invests a six-figure lump sum that's tucked away for retirement. Another invests for a new retiree who wants growth but also needs to generate some spending money now.

This isn't a contest to pick 1996's best-performing funds. Each adviser chooses funds not on forecasts of near-term returns, but because of acumen in such investment areas as emerging-growth companies or foreign stocks.

Sure, over the next year some of these funds might turn in less than sparkling results. It's rare for all kinds of funds to do well at the same time. These portfolios were designed with the current market conditions in mind but intended to fulfill long-term financial objectives. They're not cast in stone. Advisers drop funds as their clients' needs change, the portfolio managers leave, funds switch strategies—or just plain flop.

Here are our advisers' suggested mutual-fund portfolios.

■ **COLLEGE FUNDS.** It's the most daunting financial hurdle that many families will face. Many have more than one child, and at just the time the parents should start socking it away, there are other needs as well. That's why a college plan must make aggressive investments even if that means some short-term volatility.

Take the case of a three-year-old whose grandparents invest $10,000 in her name. Investment adviser Debra B. Silversmith of Sterling Partners in Denver, a fee-only advis-

Head Start on A College Fund

Investment adviser **DEBRA SILVERSMITH** suggests this portfolio for a 3-year-old whose grandparents put $10,000 in her name to get a college fund going. They're all no-load funds, available through the big discount brokers or directly from the fund companies.

FUND	ALLOCATION
OAKMARK	20.0%
STRONG OPPORTUNITY	15.0
PBHG GROWTH	25.0
BARON ASSET	15.0
WARBURG PINCUS INT'L. EQUITY COMMON	25.0

A college fund for a 3-year-old? A new retiree with a big lump sum? A good mix for an employee's 401(k)?

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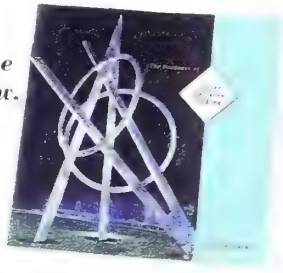

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All-Fidelity 401(k) Portfolio

Adviser **JAMES KRUZAN** counts many General Motors managers among his clients, and many of them look to him for help in choosing among the 38 Fidelity mutual funds in GM's 401(k) plan. This allocation is for a 43-year-old with $50,000 in a 401(k), but could as easily be used by anyone wanting an all-Fidelity line-up.

FUND	ALLOCATION
FIDELITY GROWTH CO. (OR FIDELITY CONTRAFUND)	10.0%
FIDELITY BLUE CHIP	20.0
FIDELITY OTC	20.0
FIDELITY SMALL CAP	20.0
FIDELITY CANADA	7.5
FIDELITY DIVERSIFIED INT'L. GROWTH	7.5
FIDELITY EUROPE	7.5
FIDELITY PACIFIC BASIN	7.5

er who uses the funds in the Schwab OneSource network, recommends a portfolio weighted toward funds emphasizing small and midsize companies whose growth prospects are higher than those of companies in the Standard & Poor's 500. "Over time, the higher growth rates should lead to greater fund performance," she says.

That's true, as long as you select funds whose managers are skilled at playing the growth-stock game. As the accompanying table shows, for the 40% of the portfolio dedicated to smaller-company stocks, she chooses Baron Asset and PBHG Growth funds. Baron, which has outperformed its rivals for nearly 10 years, is light on technology stocks. PBHG Growth, unknown until a few years ago, carries a heavy complement of tech stocks—and is run by a veteran growth-stock manager. Silversmith would prefer to have a more equal weighting between the two funds, but PBHG Growth has a $2,500 minimum initial investment. "It's a good time to buy it," she says, noting that because of the tech sell-off, it's down 7% this year. For midsize companies, Silversmith selects the Oakmark and Strong Opportunity funds. Looking abroad, she chooses Warburg Pincus International Equity Fund Common Shares, "a good mix of developed and emerging-market stocks." Adds Silversmith, "If you were going to buy one foreign fund, this is it."

Silversmith thinks this portfolio could earn an average annual return of 14%. If she's right—and that's an ambitious goal—the $10,000 will grow to more than $70,000 when this preschooler turns college freshman. Private college already costs $27,000 a year, so good fund choices are not enough—her parents will need to add money over the years.

Special Report

■ **FUNDS FOR A 401(k).** Employees often freeze when asked to choose from five or six investment options in their companies' 401(k) plans. So consider the plight of the General Motors Corp. employees, who can select from among 38 Fidelity mutual funds. That's where adviser James B. Kruzan of Investment Management & Research Inc. in Clarkston, Mich., spotted an opportunity. He has advised some 400 GM employees on fund selection for their 401(k)s.

Take, for instance, a 43-year-old executive who has amassed $50,000 in his 401(k) but has it invested in low-return fixed-income funds. He'd like to have an equity portfolio but hasn't a clue which funds to choose and in what proportions.

Since the employee is 25 years from retirement, Kruzan

A Rollover IRA

Planner **WILLIAM YOUNG** suggests this portfolio for a 50-year-old woman who is leaving a job with a $100,000 lump-sum payment that will be rolled over into an IRA. As a commission-based adviser, Young sells load funds.

FUND	ALLOCATION
PUTNAM GROWTH & INCOME A	17.0%
GUARDIAN PARK AVENUE	20.0
MFS RESEARCH A	20.0
SMALLCAP WORLD	20.0
TEMPLETON FOREIGN I	23.0

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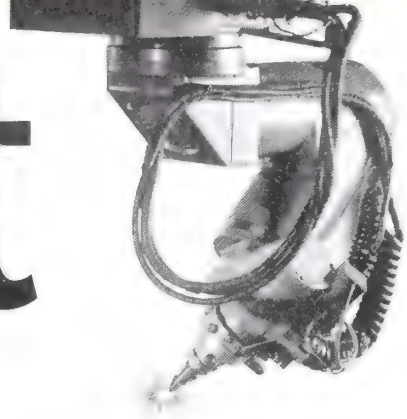

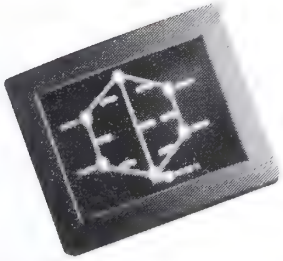

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recommends a fairly aggressive mix he believes should beat the S&P 500 by an average of two percentage points a year: 40% for funds that buy small-cap stocks, 20% for midcap, 10% for large-company, and 30% for foreign stocks. The plan could be fulfilled by scores of funds, not just Fidelity's. But for the GM clients, Kruzan selects from the Fidelity menu. For the most aggressive funds, he chooses Fidelity OTC and Fidelity Small Cap funds. For the midcap slot, he picks Fidelity Blue Chip Growth. "The name is misleading," he says. "It's really a midcap fund." The big-stock slice is a toss-up between Fidelity Growth Company and Fidelity Contrafund.

Special Report

Kruzan divides the international into four equal parts: Fidelity Canada, Europe, and Pacific Basin funds, and the Diversified International. He would choose Fidelity Japan Fund, but it's not available to the 401(k) plan. But the Pacific Basin fund is 40% invested in Japan, the diversified fund, about 25%.

For ongoing contributions, Kruzan suggests allocating money in the same proportions, with one exception: Split the foreign portion between the more volatile Diversified International and the Pacific Basin funds. "That allows you to use the market's volatility to your advantage by buying more shares at bottoms and fewer at tops," says Kruzan.

■ **ROLLOVER IRAs.** With companies shrinking payrolls, longtime employees often walk away with six-figure pension distributions and no idea of how to invest them. "That's the kind of help many of our new clients need," says William S. Young of First Financial Group in Towson, Md.

Look at the example of a 50-year-old single woman with $100,000. She's not a gambler, but she is willing to take as much risk as her adviser thinks is appropriate. So Young devised an all-equity portfolio with moderate risk. "With at least 10 years to go before retirement, you can go with an all-stock portfolio," says Young. "In all the 10-year periods since World War II, bonds have beaten stocks less than 10% of the time."

Young earns his pay from commissions—and so chooses load funds. When a fund has front-end or back-end shares, he recommends the upfront "A" or "I" shares, because they're usually most cost-effective for investors over the long term.

Young's prescription is simple: five funds, with near-equal weightings. He eschews the latest highfliers in favor of those that show "consistency of results." The first two holdings, Putnam Fund for Growth & Income A (17%) and Guardian Park Avenue (20%), are "core" funds, with Putnam having a "value" (higher dividend, low price-earnings ratio) approach, while Guardian is more oriented toward growth stocks. He also recommends MFS Research A, a growth fund whose stocks are chosen by research analysts, not portfolio managers. "The fund's not dependent on any one manager's skill," he says. Still, the fund has beaten the market over the past three- and five-year periods. "It's an underappreciated gem."

The remaining 43% of the portfolio goes to SmallCap World and Templeton Foreign I funds. That may appear to be a bit too heavy on foreign stocks. But Young says SmallCap World, despite its name, has only about one-third of its assets abroad. That, combined with Templeton Foreign, puts the portfolio's overseas investments at 30%.

■ **EQUITY FUNDS FOR RETIREMENT.** Retirement is no reason to drop equity investments. In fact, the longer you hope to live, the more you're going to need them. That's the approach adviser Madeline I. Noveck of Novos Planning Associates Inc. in New York takes in constructing a $500,000 portfolio for a 62-year-old recent retiree.

Noveck works with a large palette of funds, both no-load and load, since that affords more and better investment options. If she uses a load fund, the portion of the commission paid her is credited against her regular asset-based fees.

Noveck's list is long, with 11 funds. But she's working with more money, which usually requires more funds. The client has two needs: about $7,500 a year to supplement his income; and capital appreciation, so there will be enough to fund 20 years or so in retirement. She believes her portfolio can beat the S&P 500 return, but with less volatility.

For the Golden Years

MADELINE NOVECK recommends this portfolio for a 62-year-old with a $500,000 lump-sum pension payment. This retiree has other income sources, and needs to generate $7,500 a year from this nest egg. Most of the money is invested for long-term growth. Noveck uses both load and no-load funds.

FUND	ALLOCATION
FIDELITY ADVISOR GROWTH OPPORTUNITIES A	7.5%
HARBOR CAPITAL APPRECIATION	7.5
SIERRA EMERGING GROWTH A	4.0
THIRD AVENUE VALUE	4.0
IVY INTERNATIONAL A	23.0
COHEN & STEERS REALTY SHARES	8.0
FIDELITY ADVISOR GLOBAL RESOURCES A	7.0
VANGUARD F/I SHORT-TERM CORPORATE BOND	7.0
HARBOR BOND	18.0
T. ROWE PRICE INTERNATIONAL BOND	9.0
MONEY-MARKET FUND	5.0

Like our other advisers, Noveck covers every segment o the stock market. For large-to-midcap stocks, she chooses th Fidelity Advisor Growth Opportunities A and Harbor Capita Appreciation funds; and for small companies, Sierra Emergin Growth A and Third Avenue Value Funds. For foreign in vestments, she opts for Ivy International A, a large-cap fun focusing mainly on Europe but with some exposure to Japa and emerging markets.

Noveck also places money in funds that don't correlate t the market in general and thus diversify the portfolio. For in stance, she allocates 7% to Fidelity Advisor Global Resource A, a gold and natural-resources fund. "When the Do dropped 165 points in two days, the fund went up," sh says. Cohen & Steers Realty Shares and T. Rowe Price In ternational Bond are in the portfolio for the same reason Five percent goes to a money-market fund ("choose one wit a high yield") both for diversification and liquidity.

The realty fund has another job—to provide current in come. That, plus the income from Harbor and Vanguar bond funds, should provide the $7,500 a year the client need now—with a few dollars to spare. The distributions fro the other funds, says Noveck, should be reinvested. Tha keeps the investor's capital at work for another day.

By Jeffrey M. Laderman in New Yor

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Equity Funds

MUTUAL FUND SCOREBOARD

How to Use the Tables

BUSINESS WEEK RATING
Based on five-year risk-adjusted performance, relative to the S&P 500. Calculated by subtracting a fund's risk-of-loss factor (see RISK) from historical pretax total return. To get a positive rating, fund must beat the S&P 500 on a risk-adjusted basis. The ratings are as follows:

- ♦ ♦ ♦ SUPERIOR
- ♦ ♦ VERY GOOD
- ♦ GOOD
- AVG AVERAGE
- ♦ BELOW AVERAGE
- ♦ ♦ POOR
- ♦ ♦ ♦ VERY POOR

MANAGEMENT CHANGES
♟ indicates the fund's manager has held the job at least 10 years; ♙ indicates a new manager since Dec. 31, 1994.

S&P 500 COMPARISON
The pretax total returns for the S&P 500 are as follows: 1995, 37.5%; three-year average (1993-1995), 15.3%; five-year average (1991-95), 16.6%; 10-year average (1986-95), 14.9%.

SALES CHARGE
The cost of buying a fund, or the "load." Many load funds take the charge out of the initial investment, and for ratings purposes, performance is reduced by these charges. Loads may be levied on withdrawals, either as a flat fee or one that declines over time.

EXPENSE RATIO
Expenses for 1995 as a percentage of average net assets, a measure of how much shareholders pay for management. Footnotes indicate if a ratio includes a 12(b)-1 plan, which spends shareholder money for marketing co

OBJECTIVE
Some funds specialize in one sector, which is indicated. Others are grouped as follows: Asset allocation: mixes U.S. stocks, bonds and cash and possibly gold, real estate, and foreign securities. Multi-asset global: same as asset allocation, but always includes foreign securities. Balanced: buy

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL	% CHG. 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WITH OBJECTIV
AARP BALANCED STOCK & BOND		Balanced	277.7	56	No load	1.01	23.9	22.1	3.6	39/5
AARP CAPITAL GROWTH	♦	Growth	709.2	12	No load	0.95	30.5	29.7	1.0	141/22
AARP GROWTH & INCOME	♦ ♦	Growth/income	3259.8	42	No load	0.72	31.8	30.0	2.7	70/13
ACORN ♟	♦ ♦	Small company	2399.3	21	2.00*	0.62	20.8	18.1	0.6	80/9
ACORN INTERNATIONAL		Foreign	1276.8	–6	2.00*	1.20	8.9	8.9	0.0	38/6
AFFILIATED	♦	Growth/income	5306.6	30	5.75	0.63†	31.7	27.4	2.3	73/13
AIM AGGRESSIVE GROWTH	♦ ♦	Maximum growth	2304.1	222	5.50‡	1.07†	41.5	40.6	0.0	8/3
AIM BALANCED A	♦	Balanced	91.8	144	4.75	1.25†	35.0	34.0	2.4	1/5
AIM CHARTER A	AVG	Growth/income	2070.9	40	5.50	1.17†	35.7	31.9	1.5	36/13
AIM CONSTELLATION	AVG	Maximum growth	7377.4	99	5.50	1.20†	35.5	34.2	0.0	19/3
AIM GLOBAL AGGRESSIVE GROWTH A		World	237.6	575	4.75	2.02†	32.1	32.0	0.0	1/4
AIM GLOBAL UTILITIES A (a)	♦	Utilities	169.6	13	5.50	1.18†	27.7	26.7	3.3	14/2
AIM GROWTH A	♦ ♦	Growth	171.4	39	5.50	1.22†	34.3	32.2	0.0	99/22
AIM INTERNATIONAL EQUITY A		Foreign	705.5	8	5.50	1.64†	16.4	15.5	0.0	8/6
AIM SUMMIT	♦	Growth	1052.8	41	8.50	0.72	35.1	32.4	0.2	84/22
AIM VALUE A	♦	Growth	3397.7	150	5.50	0.98†	34.8	32.6	0.3	90/22
AIM WEINGARTEN A	♦	Growth	4562.4	24	5.50	1.20†	34.8	29.8	0.0	89/22
ALGER GROWTH	♦	Growth	172.7	120	5.00**	2.20†	38.4	36.0	0.0	39/22
ALGER SMALL CAPITALIZATION	♦ ♦	Small company	494.1	68	5.00**	2.18†	48.9	46.7	0.0	12/9
ALLIANCE A ♟	♦	Growth	896.6	22	4.25	1.05†	34.8	29.4	0.3	88/22
ALLIANCE BALANCED SHARES A	AVG	Balanced	124.7	–17	4.25	1.32†	26.6	22.4	2.5	22/9
ALLIANCE GROWTH & INCOME A	AVG	Growth/income	479.6	24	4.25	1.03†	37.9	34.4	1.7	6/11
ALLIANCE GROWTH B	♦ ♦ ♦	Growth	1679.5	107	4.00**	2.10†	28.6	27.7	0.0	159/22
ALLIANCE INTERNATIONAL A	♦ ♦ ♦	Foreign	171.9	–3	4.25	1.73†	10.1	8.3	0.0	31/
ALLIANCE PREMIER GROWTH B		Growth	239.9	75	4.00**	2.70†	45.9	42.5	0.0	8/2
ALLIANCE QUASAR A	♦ ♦	Maximum growth	158.1	22	4.25	1.83†	47.6	40.2	0.0	4/
ALLIANCE TECHNOLOGY A	AVG	Technology	385.2	79	4.25	1.66†	45.8	43.6	0.0	8/
ALLIANCE WORLDWIDE PRIVATIZATION A		World	702.1	NM	4.25	2.56†	4.9	4.9	0.0	40/
AMCAP ♟	AVG	Growth	3532.7	23	5.75	0.71†	28.7	25.4	1.1	158/2
AMCORE VINTAGE EQUITY		Growth	194.9	49	No load	1.07†	35.7	34.7	1.0	73/2
AMERICA'S UTILITY		Utilities	160.0	29	No load	1.21	32.3	30.7	3.9	6/
AMERICAN BALANCED ♟	♦ ♦	Balanced	3047.5	46	5.75	0.68†	27.1	24.5	3.8	18/
AMERICAN GAS INDEX	♦ ♦	Natural resources	212.8	21	No load	0.85	30.5	29.1	3.6	2/
AMERICAN GROWTH ♟	♦	Growth	106.0	52	5.75	1.45	25.5	24.2	1.3	199/2
AMERICAN LEADERS A	♦	Growth/income	413.1	70	6.00*	1.23	37.0	35.3	1.0	16/1
AMERICAN MUTUAL ♟	♦	Growth/income	6945.8	32	5.75	0.60†	31.4	28.4	3.3	79/1
AMERICAN NATIONAL GROWTH	♦	Growth	134.8	19	5.75	0.97	25.9	22.9	1.6	195/2
AMERICAN NATIONAL INCOME	AVG	Equity-income	141.1	23	5.75	1.12	29.1	26.4	2.7	18/
AMSOUTH BALANCED		Balanced	319.9	34	4.50	0.84	23.5	21.4	3.5	42/
AMSOUTH EQUITY	AVG	Growth	337.9	63	4.50	0.94	27.3	25.4	1.8	180/2
ARIEL APPRECIATION	♦	Growth	139.3	8	No load	1.36†	24.2	21.3	0.8	208/2
ARIEL GROWTH	♦	Small company	120.6	–8	No load	1.37†	18.5	13.7	1.4	92/
ATLAS GROWTH & INCOME A	AVG	Growth/income	93.1	34	3.00	1.04†	33.1	28.7	1.1	59/1
BABSON ENTERPRISE ♟	♦ ♦ ♦	Small company	201.9	6	No load‡	1.08	16.4	12.8	0.6	95/
BABSON GROWTH	AVG	Growth	271.1	20	No load	0.85	31.4	29.0	1.0	133/2

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not me
(a) Formerly AIM Utilities A.

stocks and bonds. Equity-
ne: emphasizes high-yield
s. Growth: strives for capital
eciation. Growth/income:
; appreciation with some
nt income. Maximum
:h: takes greater risks, and
use options, margin, or short
.

'AX TOTAL RETURN
id's net gain to investors,
ding reinvestment of divi-
s and capital gains at
h-end prices.

RTAX TOTAL RETURN
x return adjusted for federal
. Assumes ordinary income
:apital gains taxed at highest
applicable in each year; uses
tax rate on income since
. Capital gains are assumed
long-term.

)
ne distributions as a percent of net asset value, adjusted for capital gains distributions.

RANK WITHIN OBJECTIVE
1995 performance ranking relative to other funds with same objective.

TREND
A fund's relative performance during the four 30-month periods from Jan. 1, 1986 to Dec. 31, 1995. Boxes read from left to right, and the level of green indicates performance relative to all other funds in that period: ■ for the top quartile; ■ for the second quartile; ■ for the third quartile; □ for the bottom quartile. An empty box indicates no data for that period.

TURNOVER
Trading activity, the lesser of purchases or sales divided by average monthly assets.

% CASH
Portion of fund assets not invested in stocks or bonds. A negative number means the fund has borrowed to buy securities.

PRICE-EARNINGS RATIO
The average, weighted price-earnings ration of stocks in a fund's portfolio, based on last 12 month's earnings.

STYLE
Each fund has a two-letter designation describing the characteristics of the fund's portfolio. L, M, or S, stands for large-, medium-, and small-capitalization stocks. V stands for value, an investment style that emphasizes stocks with lower-than-average p-e's and price-to-book value ratios. G indicates growth stocks, which have higher p-e's and p-b's. B is a blend of the two.

UNTAXED GAINS
Percentage of assets in portfolio that are unrealized and undistributed capital gains. A negative figure indicates losses that may offset future gains.

LARGEST HOLDING
Comes from the latest available fund reports.

RISK
Potential for losing money in a fund, or risk-of-loss factor. For each fund, the three-month Treasury bill return is subtracted from the monthly total return for each of the 60 months in the ratings period. When a fund has not performed as well as Treasury bills, the monthly result is negative. The sum of these negative numbers is divided by the number of months. The result is a negative number, and the greater its magnitude, the higher the risk of loss. This number is the basis for BW ratings and the RISK column.

AGE ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
'EARS AFTERTAX	5 YEARS PRETAX	5 YEARS AFTERTAX	10 YEARS PRETAX	10 YEARS AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE	
nd, not rated						Average	19	19	LB	12	United Technologies(2)		322-2282	MA	617-330-5400
9.6	14.9	13.6	12.8	11.1		High	2	20	LB	23	FNMA(3)	High	322-2282	MA	617-330-5400
14.6	16.8	15.1	13.7	11.8		Low	0	19	LB	25	Eli Lilly(3)	Low	322-2282	MA	617-330-5400
12.0	22.0	20.3	15.6	12.9		Low	4	23	SB	42	Solectron(2)	Average	922-6769		
16.0						Low	3	22	SG	11	WM Data Nordic(2)		922-6769		
12.4	16.3	13.2	13.5	9.9		Average	4	20	LV	26	SmithKline Beecham (Unit)ADR(3)	Low	874-3733	NY	212-848-1800
29.6	34.2	32.5	17.3	15.9		Average	0	31	SG	27	Oak Technology(1)	High	347-1919	TX	713-626-1919
12.9	18.2	17.3	9.9	8.1		Average	8	20	LB	15	Texas Instruments(2)	Average	347-1919	TX	713-626-1919
10.3	14.6	12.9	14.8	11.6		High	–1	19	LB	23	Philip Morris(3)	Average	347-1919	TX	713-626-1919
16.5	25.8	25.3	20.4	17.2		Average	8	29	MG	32	LSI Logic(1)	High	347-1919	TX	713-626-1919
nd, not rated							10	25	SG	13	Telecom de Argentina Cl B(1)		347-1919	TX	713-626-1919
6.8	11.1	8.8				High	1	15	MV	3	Northern States Power(3)	Average	347-1919	TX	713-626-1919
7.7	12.7	9.5	11.1	7.7		Very high	9	25	MG	30	Applied Materials(1)	High	347-1919	TX	713-626-1919
17.2						Average	3	25	MG	18	Hanjaya Mandala Sampoerna(1)		347-1919	TX	713-626-1919
10.4	16.4	14.1	13.7	11.4		High	1	23	MB	30	IBM(2)	High	347-1919	TX	713-626-1919
17.0	22.5	20.3	17.8	14.8		High	1	18	MV	22	Texas Instruments(5)	Average	347-1919	TX	713-626-1919
8.1	14.6	12.8	15.8	13.5		High	3	22	MB	31	Applied Materials(2)	High	347-1919	TX	713-626-1919
15.9	21.1	19.3				High	10	28	MG	28	Altera(3)	High	992-3863	NY	201-547-8320
15.3	20.8	19.4				High	5	31	MG	41	Glenayre Technologies(4)	Very high	992-3863	NY	201-547-8320
10.3	18.2	14.4	14.1	9.0		Average	2	19	LB	30	Philip Morris(6)	High	227-4618	NJ	201-319-4000
7.4	11.0	9.3	10.1	7.2		Very high	16	23	LG	19	Philip Morris(3)	Low	227-4618	NJ	201-319-4000
10.5	14.0	11.3	13.0	8.4		Average	3	21	LB	22	Philip Morris(5)	Average	227-4618	NJ	201-319-4000
15.8	23.8	21.3				Average	4	24	LB	13	Cisco Systems(6)	Average	227-4618	NJ	201-319-4000
12.1	8.5	7.3	11.3	8.1		High	0	28	LB	10	Rohm(2)	High	227-4618	NJ	201-319-4000
12.9						Average	2	21	LB	27	Philip Morris(7)		227-4618	NJ	201-319-4000
12.5	17.0	14.1	11.4	8.5		High	7	30	SG	44	Nine West Group(4)	High	227-4618	NJ	201-319-4000
26.8	32.3	28.0	18.8	15.6		Average	17	26	MG	50	Intel(4)	High	227-4618	NJ	201-319-4000
nd, not rated						Low	2	18	MV	1	SEITA-Ste Nationale Tabacs(2)		227-4618	NJ	201-319-4000
9.2	15.9	13.3	13.6	10.7		Low	17	23	LB	38	Time Warner(4)	Average	421-4120	CA	213-486-9200
12.7						Low	1	21	LB	24	Motorola(2)		438-6375		
7.7						Low	0	17	MV	4	CINergy(4)		487-3863	VA	804-649-1315
10.2	14.1	11.9	12.3	9.1		Low	18	20	LV	14	Philip Morris(2)	Very low	421-4120	CA	415-421-9360
9.9	9.6	8.2				Very low	2	19	MV	8	Consolidated Natural Gas(5)	Average	343-3355	MD	301-657-1500
10.8	15.9	12.8	11.2	8.2		Very high	3	18	LB	13	UAL(6)	Average	525-2406	CO	303-623-6137
13.8	17.5	15.6	12.7	10.1		Low	4	18	LB	26	Consolidated Rail(3)	Low	245-5051	PA	412-288-1561
11.9	14.6	12.0	13.0	10.0		Low	21	17	LV	28	AT&T(2)	Low	421-4120	CA	213-486-9200
8.7	13.5	10.3	11.6	8.1		Average	10	21	LB	20	J. P. Morgan(3)	Average	231-4639	TX	409-763-8272
8.9	13.5	10.5	11.6	8.4		Average	9	20	LB	18	American Home Products(3)	Low	231-4639	TX	409-763-8272
10.1						Very low	7	20	LV	14	AmSouth Prime Obligations(5)		451-8379	OH	205-581-7530
13.2	14.8	13.0				Very low	7	20	LV	17	IBM(3)	Average	451-8379	OH	205-581-7530
5.4	13.1	11.9				Low	3	22	SB	23	Rouse(4)	Average	292-7435	IL	312-726-0140
4.5	12.9	10.3				Very low	2	22	SB	38	Longs Drug Stores(5)	Average	292-7435	IL	312-726-0140
11.1	15.2	13.7				High	19	22	MB	22	Bush Boake Allen(1)	Average	933-2852		
8.6	19.8	16.6	12.8	9.9		Very low	3	22	SV	23	Nichols Research(3)	Low	422-2766	MO	816-471-5200
10.8	14.7	13.0	12.1	8.8		Low	3	22	LB	45	Philip Morris(4)	Low	422-2766	MO	816-471-5200

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG. 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WITHIN OBJECTIVE
BABSON VALUE	♦♦	Growth/income	308.3	153	No load	0.99	31.7	30.6	1.8	72/138
BAILARD BIEHL & KAISER INTL. EQUITY	♦♦♦	Foreign	107.9	–27	No load	1.53	12.5	9.5	0.9	17/66
BARON ASSET	♦	Small company	353.1	306	No load	1.40†	35.3	35.2	0.0	32/99
BARTLETT BASIC VALUE	♦	Growth/income	122.8	32	No load	1.20	31.6	29.2	1.7	76/138
BENHAM EQUITY GROWTH		Growth	159.3	63	No load	0.75	34.6	31.5	1.5	91/229
BENHAM GOLD EQUITIES INDEX	♦♦♦	Precious metals	540.4	–5	No load	0.61	9.3	9.2	0.1	5/15
BENHAM INCOME & GROWTH	♦♦	Growth/income	373.7	66	No load	0.73	36.9	34.4	2.3	17/138
BENHAM UTILITIES INCOME		Utilities	217.4	43	No load	0.75	35.3	33.9	3.3	2/26
BERGER 100	♦	Growth	2152.3	2	No load	1.48†	21.3	19.7	0.0	221/229
BERGER 101	AVG	Growth/income	349.9	–5	No load	1.63†	23.9	23.4	1.4	131/138
BERGER SMALL COMPANY GROWTH		Small company	570.9	96	No load	1.89†	33.8	33.8	0.0	39/99
BERNSTEIN INTERNATIONAL VALUE		Foreign	2169.3	52	No load	1.39	8.1	7.2	0.6	44/66
BERWYN	♦♦	Small company	97.2	53	1.00*	1.33	19.2	16.7	7.5	87/99
BERWYN INCOME	♦♦♦	Asset allocation	119.6	114	No load‡	0.93	21.1	18.1	8.5	26/34
BILTMORE BALANCED		Balanced	210.5	9	4.50	0.75	27.7	25.5	3.2	14/57
BILTMORE EQUITY		Growth/income	134.8	53	4.50	0.89	31.5	28.7	1.9	78/138
BILTMORE EQUITY INDEX		Growth/income	193.2	18	4.50	0.49	36.8	33.8	2.0	18/138
BILTMORE QUANTITATIVE EQUITY		Growth	121.6	33	4.50	0.92	38.6	37.1	1.7	34/229
BNY HAMILTON EQUITY-INCOME		Equity-income	169.8	26	3.00	1.04†	25.8	24.5	2.4	27/34
BRAMWELL GROWTH		Growth	137.9	927	No load	1.75†	32.5	32.5	0.0	121/229
BRANDYWINE	AVG	Growth	4210.5	83	No load	1.07	35.7	31.2	0.0	72/229
BT INVESTMENT EQUITY 500 INDEX		Growth/income	276.1	53	No load	0.25	37.1	36.1	2.1	13/138
BT INVESTMENT EQUITY APPREC.		Growth	109.4	265	No load	1.00	37.6	36.6	0.0	50/229
BT INVESTMENT SMALL CAP		Small company	162.3	411	No load	1.25	58.6	55.5	0.0	4/99
BURNHAM A	AVG	Growth/income	112.0	10	5.00	1.50†	24.4	22.4	3.2	130/138
CALVERT SOCIAL INVMNT. EQUITY A	♦♦	Growth	91.9	5	4.75	1.36†	21.5	18.2	1.2	220/229
CALVERT SOCIAL INVMNT. MANAGED A	AVG	Balanced	574.2	17	4.75	1.24†	25.9	21.0	2.5	27/57
CALVERT STRATEGIC GROWTH A		Maximum growth	135.8	73	4.75	2.55†	2.9	2.2	1.4	34/34
CALVERT WORLD VALUES GLOB. EQTY. A		World	190.4	8	4.75	1.96†	11.8	10.8	0.8	29/41
CAPITAL INCOME BUILDER	♦	Multi-asset global	4809.0	34	5.75	0.73†	25.1	22.8	4.6	3/18
CAPITAL WORLD GROWTH & INCOME		World	3723.4	32	5.75	0.87†	21.4	19.8	3.0	7/41
CARDINAL	AVG	Growth/income	231.3	1	4.50	0.70	27.3	23.6	2.6	117/138
CENTURY SHARES	AVG	Financial	267.2	30	No load	1.01	35.2	33.4	1.4	7/7
CGM CAPITAL DEVELOPMENT	♦	Growth	521.2	30	No load‡	0.84	41.0	38.7	0.1	22/229
CGM MUTUAL	AVG	Balanced	1154.4	9	No load	0.92	24.3	22.3	2.5	38/57
CHESAPEAKE GROWTH		Growth	425.4	81	3.00‡	1.43	30.2	27.6	0.0	146/229
CHICAGO TRUST GROWTH & INCOME (b)		Growth/income	183.2	NM	No load	1.20†	35.6	35.0	0.7	38/138
CLIPPER	♦	Growth	403.5	63	No load	1.11	45.2	41.4	1.1	10/229
COHEN & STEERS REALTY SHARES		Real estate	793.1	73	No load	1.14	11.1	9.4	5.3	1/3
COLONIAL A	♦	Growth/income	682.0	27	5.75	1.14†	28.6	25.3	2.2	110/138
COLONIAL GLOBAL UTILITIES A (c)		Utilities	213.7	–12	5.75	1.20†	18.0	16.5	4.5	25/26
COLONIAL GROWTH SHARES A	AVG	Growth	197.9	31	5.75	1.22†	38.0	34.7	1.0	46/229
COLONIAL NEWPORT TIGER T (d)	♦	Pacific	195.7	–57	5.75‡	1.29	16.3	16.0	0.7	1/22
COLONIAL U.S. FUND FOR GROWTH B		Growth	259.9	56	5.00**	2.21†	28.5	25.6	0.4	162/229
COLONIAL UTILITIES B		Utilities	855.9	16	5.00**	1.98†	33.8	32.3	3.5	5/26
COLUMBIA BALANCED		Balanced	486.8	95	No load	0.72	25.0	22.5	3.5	34/57
COLUMBIA COMMON STOCK		Growth/income	358.5	189	No load	0.84	30.8	28.5	1.3	84/138
COLUMBIA GROWTH	AVG	Growth	848.7	43	No load	0.81	32.9	29.3	0.9	115/229
COLUMBIA INTERNATIONAL STOCK		Foreign	100.9	–15	No load	1.52	5.1	5.1	0.0	51/66
COLUMBIA SPECIAL	AVG	Small company	1384.4	56	No load	1.05	29.3	25.2	0.1	55/99
COMMERCE GROWTH		Growth	149.4	NM	3.50	NA	39.1	37.1	0.7	32/229
COMMON SENSE GROWTH	♦	Growth	2335.4	20	8.50	1.09	32.8	27.5	1.0	117/229
COMMON SENSE GROWTH & INCOME	AVG	Growth/income	795.7	31	8.50	1.02	36.6	32.1	1.9	22/138
COMPOSITE BOND & STOCK A	♦♦	Balanced	221.9	21	4.50	1.02†	31.2	29.0	3.5	4/57
COMPOSITE GROWTH & INCOME A (e)	♦	Growth/income	142.0	42	4.50	1.07†	33.1	31.3	1.4	58/138
COMPOSITE NORTHWEST A (f)	♦♦	Growth	161.2	10	4.50	1.10†	26.5	26.0	0.4	189/229
COMSTOCK PARTNERS STRATEGY O	♦	Multi-asset global	249.6	–32	4.50‡	1.14†	4.4	2.7	5.3	17/18
CONNECTICUT MUT. GROWTH A	♦♦	Growth	118.8	52	5.00	1.02†	36.4	33.4	1.3	60/229
CONNECTICUT MUT. TOTAL RETURN A	♦♦	Asset allocation	218.7	23	5.00	0.96†	24.0	21.4	3.7	19/34
CRABBE HUSON ASSET ALLOCATION	♦♦	Asset allocation	142.9	33	No load	1.44†	20.2	16.7	2.3	28/34
CRABBE HUSON EQUITY	♦♦♦	Growth	429.1	176	No load	1.45†	26.4	23.6	2.9	191/229
CRABBE HUSON SPECIAL	♦	Maximum growth	919.2	143	No load	1.44†	10.8	9.1	1.4	33/34
DAVIS NY VENTURE A (g)	AVG	Growth	1798.2	65	4.75	0.90†	40.6	37.6	1.0	24/229
DEAN WITTER AMERICAN VALUE	AVG	Growth	2383.2	60	5.00**	1.71†	42.2	38.2	4.3	15/229
DEAN WITTER CAPITAL GROWTH	♦♦	Growth	512.9	17	5.00**	1.87†	31.3	31.3	0.0	134/229
DEAN WITTER DEVELOPING GROWTH	♦♦	Small company	571.5	69	5.00**	1.77†	47.7	44.6	0.0	14/99
DEAN WITTER DIVIDEND GROWTH	♦	Growth/income	9369.0	40	5.00**	1.42†	34.9	34.1	1.7	46/138
DEAN WITTER EUROPEAN GROWTH	♦	Europe	890.4	23	5.00**	2.27†	24.6	22.8	0.0	1/11
DEAN WITTER GLOBAL DIV. GRTH. SECS.		World	2238.4	29	5.00**	1.97†	19.9	18.2	1.2	12/41
DEAN WITTER GLOBAL UTILITIES		Utilities	355.2	3	5.00**	1.97†	14.3	13.4	1.4	26/26

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not meanin
(b) Formerly CT&T Growth & Income. (c) Formerly Liberty Financial Utilities. (d) Formerly Newport Tiger. (e) Formerly Composite Growth A. (f) Formerly Composite Northwest 50 A.
(g) Formerly New York Venture A.

AVERAGE ANNUAL TOTAL RETURNS (%)						TREND	PORTFOLIO DATA						RISK	TELEPHONE		
3 YEARS		5 YEARS		10 YEARS		BW 10-YEAR	TURNOVER	%CASH	P-E	STYLE	UNTAXED	LARGEST HOLDING		TOLL-FREE	IN-STATE	
RETAX	AFTERTAX	PRETAX	AFTERTAX	PRETAX	AFTERTAX	ANALYSIS			RATIO		GAINS (%)	COMPANY (% ASSETS)		(800)		
8.4	16.9	19.8	18.4	14.4	12.7		Very low	7	19	LV	17	SLMA(3)	Low	422-2766	MO	816-471-5200
0.7	9.7	4.1	3.3	7.7	3.7		Very high	7	25	LV	9	Royal Dutch Petroleum (Neth)(3)	High	882-8383	CA	415-571-5800
1.5	20.8	22.3	21.8				Low	1	27	SG	23	Robert Half International(7)	Average	992-2766	NY	212-759-7700
3.8	12.0	15.4	13.8	11.1	8.7		Low	7	20	MV	24	Multimedia(3)	Low	800-4612	OH	513-621-4612
4.4	12.2						High	9	17	LV	19	Atlantic Richfield(3)		331-8331	CA	415-965-4274
8.1	18.1	6.0	5.9				Average	0	43	MG	8	Barrick Gold(23)	Very high	331-8331	CA	415-965-4274
4.9	12.9	17.8	16.2				Average	1	17	LV	21	General Electric(4)	Low	331-8331	CA	415-965-4274
w fund, not rated							Average	1	16	LV	5	BellSouth(4)		331-8331	CA	415-965-4274
1.1	10.6	23.0	22.5	18.7	16.9		High	8	31	MG	26	CUC International(2)	High	333-1001	CO	303-329-0200
1.7	11.3	18.6	17.7	11.8	9.9		Average	8	23	LB	16	Johnson & Johnson(3)	Average	333-1001	CO	303-329-0200
w fund, not rated							High	10	38	SG	23	Glenayre Technologies(1)		333-1001	CO	303-329-0200
4.7	13.8						Low	7	27	MV	5	Fuji Photo Film(3)			NY	212-756-4097
5.1	13.4	21.4	19.6	12.9	10.8		Low	2	16	SV	21	Printronix(4)	Average	824-2249	PA	610-640-4330
1.9	9.0	16.1	12.9				Low	1	14	SV	6	Coachmen Industries(16)	Very low	824-2249	PA	610-640-4330
w fund, not rated							Average	6	20	LB	13	Philip Morris(1)		462-7538		
w fund, not rated								9	20	LV	14	FMC(2)		462-7538		
w fund, not rated								0	20	LB	25	General Electric(2)		462-7538		
w fund, not rated								1	17	LV	20	General Electric(3)		462-7538		
1.2	10.1						Average	9	22	LB	13	Exxon(2)		426-9363		
w fund, not rated							Average	1	25	MG	11	Eckerd(4)		272-6227		
8.5	15.4	23.5	20.7	18.6	16.4		Very high	7	27	MG	15	Cisco Systems(6)	High	656-3017	DE	302-656-6200
5.0	13.9						Low	1	20	LB	19	General Electric(2)		730-1313		
w fund, not rated							High	5	33	MG	22	Glenayre Technologies(2)		730-1313		
w fund, not rated								12	38	SG	24	Dollar Tree Stores(2)		730-1313		
0.2	7.8	11.2	8.9	11.5	8.3		High	3	18	LB	14	Chrysler(3)	Low	874-3863	NY	212-262-3100
3.0	1.2	7.6	6.3				Low	7	18	LV	3	Black & Decker(5)	High	368-2748	MO	301-951-4820
8.3	6.1	10.0	8.0	10.3	8.3		Low	18	23	LB	13	Philips Electronics (ADR)(2)	Very low	368-2748	MO	301-951-4820
w fund, not rated							Very low	74	44	MG	4	Gold Bars(5)		368-2748	MO	301-951-4820
1.0	9.8						Average	10	27	LB	1	Hysan Development(2)		368-2748	MO	301-951-4820
2.1	10.3	14.3	12.4				Low	24	14	LV	13	American Home Products(3)	Very low	421-4120	CA	213-486-9200
w fund, not rated							Low	11	17	LV	14	Int'l. Nederlander Groep(3)		421-4120	CA	213-486-9200
9.3	6.7	13.7	11.3	11.8	9.3		Low	9	16	LV	38	Cincinnati Financial(4)	Low	848-7734	OH	614-464-6852
9.0	7.3	16.7	15.0	12.7	10.1		Very low	5	15	MV	64	General Re(7)	Average	321-1928	MA	617-482-3060
1.8	8.6	26.8	21.7	19.2	14.5		High	1	13	LV	20	Citicorp(7)	Very high	345-4048	MA	617-859-7714
1.0	9.0	15.4	12.7	13.9	10.8		Very high	1	12	LV	12	Citicorp(8)	Average	345-4048	MA	617-859-7714
w fund, not rated							Average	1	23	SB	31	KLA Instruments(3)		525-3863		
w fund, not rated								7	22	LB	12	Microsoft(3)		992-8151		
6.4	13.3	19.3	16.5	14.9	12.1		Average	22	17	LV	29	FNMA(10)	Average	776-5033	CA	310-247-3940
2.6	10.5						Average	3	22	SB	1	Rouse(5)		437-9912	NY	212-832-3232
3.0	10.5	15.4	13.2	12.8	10.2		Average	5	16	LV	23	Conrail(3)	Low	248-2828	MA	617-426-3750
8.1	6.4						Low	2	18	MV	0	PowerGen (ADR)(2)		248-2828	MA	617-426-3750
3.9	10.8	17.1	14.4	14.5	11.0		High	9	20	MB	26	Loews(4)	Average	248-2828	MA	617-426-3750
1.5	21.2	22.5	22.3				Very low	9	19	LG	63	Hong Kong & China Gas(4)	High	248-2828	MA	617-426-3750
2.9	11.1						Average	4	17	LV	20	Exxon(4)		248-2828	MA	617-426-3750
8.9	7.5						Very low	2	16	LV	–4	NYNEX(4)		248-2828	MA	617-426-3750
2.5	10.6						High	6	24	LB	11	Royal Dutch Petroleum (ADR)(1)		547-1707	OR	503-222-3606
5.8	14.1						Average	1	24	LB	15	Service International(3)		547-1707	OR	503-222-3606
4.3	11.5	17.6	14.5	14.4	10.5		Average	1	26	LG	24	Apria HealthCare Group(4)	Average	547-1707	OR	503-222-3606
1.0	10.6						High	3	28	LB	6	Bombardier Cl B(2)		547-1707	OR	503-222-3606
7.2	13.7	22.4	19.6	18.5	16.2		Very high	2	31	MG	20	Adobe Systems(2)	Average	547-1707	OR	503-222-3606
w fund, not rated								NA	NA			NA		305-2140		
2.4	9.2	16.1	13.0				High	7	23	LB	22	American Cap Small Cap Fund(4)	Average	544-5445		
3.0	9.6	15.3	12.6				High	7	22	LB	22	Royal Dutch Petroleum (ADR)(2)	Average	544-5445		
1.9	10.2	13.4	11.4	10.6	8.3		Low	3	21	LB	20	FNMA(2)	Very low	543-8072	WA	509-353-3550
3.4	11.4	15.5	13.5	11.9	9.3		Average	0	22	LB	27	Microsoft(3)	Low	543-8072	WA	509-353-3550
8.5	7.9	13.9	13.4				Very low	1	25	MB	36	Microsoft(9)	High	543-8072	WA	509-353-3550
6.9	4.8	6.3	4.0				High	1	53	MG	–5	Placer Dome(4)	Low	645-6561	MA	718-895-1206
7.9	15.0	20.2	17.0	14.8	11.9		High	9	16	LV	24	Loral(2)	Average	234-5606		
2.0	9.6	14.7	11.9	12.0	9.4		High	24	18	LV	13	Loral(1)	Very low	234-5606		
2.1	9.6	13.9	11.6				High	11	23	MV	12	Louisiana Pacific(2)	Very low	541-9732	OR	503-295-0919
7.4	15.7	20.6	18.6				High	14	23	MV	9	Louisiana Pacific(3)	Low	541-9732	OR	503-295-0919
8.5	17.2	21.0	17.9				High	16	26	SB	2	Rollins Environmental Svcs.(3)	High	541-9732	OR	503-295-0919
7.0	14.9	20.3	18.1	17.0	13.5		Very low	9	18	LV	34	American Express(3)	Average	279-0279	NM	505-983-4335
6.3	14.3	20.6	18.7	15.4	13.3		Very high	4	29	MG	29	Boeing(2)	High	869-3863	NY	212-392-2550
5.0	4.0	11.3	10.5				Very low	0	23	LG	16	FNMA(2)	Average	869-3863	NY	212-392-2550
2.6	21.0	21.6	20.7	12.2	11.7		High	12	34	MG	38	LSI Logic(2)	Very high	869-3863	NY	212-392-2550
4.3	13.5	15.6	14.7	13.5	12.0		Very low	5	17	LB	34	Schering-Plough(2)	Low	869-3863	NY	212-392-2550
2.6	20.8	14.1	12.8				Average	3	18	LB	22	British Telecommunications(2)	High	869-3863	NY	212-392-2550
w fund, not rated							Low	0	22	LV	10	Philip Morris(2)		869-3863	NY	212-392-2550
w fund, not rated								15	22	LB	8	BBC Brown Boveri (Br)(3)		869-3863	NY	212-392-2550

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG. 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WITHIN OBJECTIVE
DEAN WITTER HEALTH SCIENCES		Health care	360.8	48	5.00**	2.30†	62.3	59.4	0.0	1/9
DEAN WITTER INTL. SMALL CAP		Foreign	109.2	12	5.00**	2.90†	2.9	2.9	0.0	55/66
DEAN WITTER MID-CAP GROWTH		Growth	203.1	130	5.00**	2.21†	41.3	38.0	0.0	17/229
DEAN WITTER NAT. RESOURCE DEV. SEC.		Natural resources	149.9	10	5.00**	1.90†	23.4	21.6	0.3	6/11
DEAN WITTER PACIFIC GROWTH		Pacific	1467.1	3	5.00**	2.41†	4.0	3.2	2.3	10/22
DEAN WITTER STRATEGIST	AVG	Asset allocation	1262.7	65	5.00**	1.63†	24.3	21.0	1.9	17/34
DEAN WITTER UTILITIES	AVG	Utilities	3323.0	17	5.00**	1.64†	28.4	26.9	3.8	13/26
DEAN WITTER VALUE-ADDED MKT. EQTY.		Growth/income	806.8	63	5.00**	1.64†	29.0	28.4	1.0	108/138
DEAN WITTER WORLD WIDE INVMNT.		World	498.2	–13	5.00**	2.41†	4.6	4.6	0.0	41/41
DELAWARE A		Balanced	510.7	15	4.75	0.97†	25.9	22.9	3.1	26/57
DELAWARE DECATUR INCOME A	AVG	Equity-income	1404.4	21	4.75	0.81†	32.9	28.9	3.6	9/34
DELAWARE DECATUR TOTAL RET. A	AVG	Growth/income	550.0	36	4.75	1.26†	36.5	32.5	2.3	26/138
DELAWARE DELCAP A		Growth	860.5	5	4.75	1.35†	29.8	25.4	0.0	149/229
DELAWARE TREND A		Maximum growth	399.3	49	4.75	1.36†	42.5	40.3	0.0	6/34
DELAWARE VALUE A		Small company	180.5	3	5.75	1.46†	23.5	21.8	1.0	73/99
DG EQUITY		Growth	359.9	55	3.50	0.95†	35.0	33.1	1.2	86/229
DODGE & COX BALANCED		Balanced	1800.3	148	No load	0.58	28.0	25.9	3.9	13/57
DODGE & COX STOCK		Growth/income	1227.9	126	No load	0.61	33.4	31.2	2.0	54/138
DREYFUS		Growth/income	2654.7	8	No load	0.74	23.8	13.4	1.5	132/138
DREYFUS APPRECIATION	AVG	Growth	460.7	97	No load	0.96	37.9	37.2	1.6	48/229
DREYFUS BALANCED		Balanced	196.3	112	No load	1.04	25.0	22.1	3.5	33/57
DREYFUS CAP. VALUE A (PREMIER)		Multi-asset global	250.5	–30	4.50	1.21	–3.1	–4.4	4.4	18/18
DREYFUS CORE VALUE INV.	AVG	Growth	402.2	26	No load	1.11†	35.6	31.9	1.4	76/229
DREYFUS GLOBAL GROWTH		World	108.9	–21	3.00	1.40	12.1	12.1	0.0	28/41
DREYFUS GROWTH & INCOME		Growth/income	1860.1	15	No load	1.14	25.0	23.2	2.3	128/138
DREYFUS GROWTH OPPORTUNITY		Growth	408.6	12	No load	1.10	28.4	23.5	1.2	165/229
DREYFUS INTL. EQUITY		Foreign	107.2	–33	No load	1.92†	0.7	0.7	0.0	59/66
DREYFUS MIDCAP INDEX (h)		Growth	128.6	72	1.00*	0.40	30.3	28.2	1.5	145/229
DREYFUS NEW LEADERS		Small company	608.2	55	1.00*	1.16	29.8	27.0	0.2	53/99
DREYFUS S&P 500 INDEX (i)		Growth/income	365.4	56	1.00*	0.61	36.7	35.6	1.7	20/138
DREYFUS THIRD CENTURY		Growth	419.3	20	No load	1.12	35.8	33.1	0.5	70/229
ECLIPSE FINANCIAL ASSET EQUITY	AVG	Small company	174.8	–10	No load	1.12	19.7	18.3	0.5	85/99
ENTERPRISE CAPITAL APPREC A		Growth	121.3	20	4.75	1.66†	25.7	22.4	0.0	197/229
ENTERPRISE GROWTH A		Growth	122.4	38	4.75	1.60†	40.0	38.5	0.0	26/229
EUROPACIFIC GROWTH		Foreign	10922.3	32	5.75	0.97†	12.9	11.9	2.1	15/66
EV MARATHON GREATER CHINA GROWTH		Pacific	304.3	46	5.00**	2.38†	3.2	3.2	0.0	13/22
EV TRADITIONAL GROWTH		Growth	135.5	13	4.75	0.95†	29.2	27.9	0.3	153/229
EV TRADITIONAL INVESTORS		Balanced	236.6	18	4.75	0.91†	29.7	27.1	3.0	6/57
EV TRADITIONAL STOCK		Growth/income	99.2	18	4.75	0.98†	32.8	28.4	1.7	63/138
EV TRADITIONAL TOTAL RETURN		Utilities	456.7	2	4.75	1.18†	27.4	25.1	4.3	16/26
EVERGREEN BALANCED B (j)		Balanced	109.0	9	5.00**	1.48†	25.5	23.2	3.0	29/57
EVERGREEN UTILITY A (k)		Utilities	108.2	NM	4.75	0.53†	30.7	27.7	3.9	10/26
EVERGREEN VALUE A (l)	AVG	Growth	292.4	55	4.75	0.93†	31.8	29.3	2.4	128/229
EXCELSIOR EQUITY (m)		Growth	172.0	49	4.50	1.05	28.9	25.6	0.4	156/229
EXCELSIOR INCOME & GROWTH (n)		Growth/income	118.9	21	4.50	1.06	30.0	28.9	2.2	97/138
FAM VALUE		Small company	266.3	27	No load	1.39	19.7	18.9	0.8	84/99
FEDERATED GROWTH STRATEGIES A (o)		Growth	245.5	–13	5.50	0.99	40.0	32.1	0.6	25/229
FEDERATED INDEX MINI-CAP		Small company	134.2	31	No load	0.73	26.4	24.1	1.1	67/99
FEDERATED INTL. EQUITY A (p)		Foreign	182.9	–26	5.50	1.61	6.5	3.3	0.5	47/66
FEDERATED STOCK		Growth/income	665.4	20	No load	0.97	35.6	32.5	1.4	37/138
FIDELITY		Growth/income	3213.7	70	No load	0.64	32.8	29.9	1.7	62/138
FIDELITY ADVISOR EQUITY GROWTH A		Growth	2099.8	131	3.50	1.70†	39.1	37.2	0.2	31/229
FIDELITY ADVISOR EQUITY INCOME A		Equity-income	956.3	369	3.50	1.64†	32.5	31.2	1.6	10/34
FIDELITY ADVISOR GLOBAL RESOURCES A		Natural resources	315.7	63	3.50	2.07†	28.7	27.5	0.0	3/11
FIDELITY ADVISOR GROWTH OPPORT. A		Growth	10946.2	127	3.50	1.62†	33.0	32.1	1.3	113/229
FIDELITY ADVISOR INCOME & GROWTH A		Balanced	3488.5	10	3.50	1.58†	14.1	12.7	3.9	57/57
FIDELITY ADVISOR OVERSEAS A		Foreign	803.4	22	3.50	1.90†	8.6	8.4	0.6	39/66
FIDELITY ADVISOR STRAT. OPPTY. A		Growth	615.0	63	3.50	1.84†	38.1	36.6	1.5	45/229
FIDELITY ASSET MANAGER		Multi-asset global	11165.4	1	No load	0.97	18.2	17.1	2.9	13/18
FIDELITY ASSET MANAGER: GROWTH		Multi-asset global	2894.6	1	No load	1.15	20.0	19.4	1.5	10/18
FIDELITY ASSET MANAGER: INCOME		Asset allocation	600.7	26	No load	0.79	16.7	15.1	4.6	32/34
FIDELITY BALANCED		Balanced	4880.1	–2	No load	0.90	14.9	13.4	4.2	56/57
FIDELITY BLUE CHIP GROWTH		Growth	7801.9	137	3.00	1.02	28.4	25.5	0.4	164/229
FIDELITY CANADA		Foreign	174.7	–48	4.00*	1.57	19.4	19.2	0.4	5/66
FIDELITY CAPITAL APPRECIATION	AVG	Maximum growth	1669.1	3	3.00	1.06	18.8	16.1	2.2	32/34
FIDELITY CONTRAFUND		Growth	14831.7	71	3.00	1.00	36.3	33.3	0.2	61/229
FIDELITY DESTINY I		Growth	4278.7	33	8.24	0.68	37.0	34.5	2.2	54/229
FIDELITY DESTINY II		Growth	2207.5	50	8.24	0.80	36.0	34.1	2.0	68/229
FIDELITY DISCIPLINED EQUITY		Growth	2145.6	85	No load	0.93	29.0	25.0	1.3	155/229
FIDELITY DIVERSIFIED INTERNATIONAL		Foreign	340.7	11	No load	1.25	18.0	16.4	1.7	7/66

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not meaningful. (h) Formerly Peoples S&P MidCap Index. (i) Formerly Peoples Index. (j) Formerly First Union Balanced C Invmt. (k) Formerly First Union Utility B Invmt. (l) Formerly First Union Value B Invmt. (m) Formerly UST Master Equity. (n) Formerly UST Master Income & Growth. (o) Formerly Federated Growth. (p) Formerly FT International Equity A.

AVERAGE ANNUAL TOTAL RETURNS (%)						TREND	PORTFOLIO DATA						RISK	TELEPHONE		
3 YEARS		5 YEARS		10 YEARS		BW 10-YEAR	TURNOVER	%CASH	P-E	STYLE	UNTAXED	LARGEST HOLDING		TOLL-FREE	IN-STATE	
TAX	AFTERTAX	PRETAX	AFTERTAX	PRETAX	AFTERTAX	ANALYSIS			RATIO		GAINS (%)	COMPANY (% ASSETS)		(800)		
.0	16.3						High	0	40	SG	27	IDEXX Laboratories(3)		869-3863	NY	212-392-2550
v fund, not rated								7	27	SB	–8	Kiekert(1)		869-3863	NY	212-392-2550
v fund, not rated								6	33	MG	22	Analog Devices(2)		869-3863	NY	212-392-2550
.8	10.7	10.3	8.5	10.8	9.1		Average	2	25	LB	12	Exxon(5)	High	869-3863	NY	212-392-2550
.6	17.7	16.0	15.3				Low	1	23	MG	5	Hutchison Whampoa(3)	Very high	869-3863	NY	212-392-2550
.6	7.6	13.3	11.6				Very high	3	22	LB	17	Cisco Systems(1)	Low	869-3863	NY	212-392-2550
.3	7.7	11.0	9.4				Very low	1	17	LV	16	AT&T(2)	Low	869-3863	NY	212-392-2550
.3	12.7	16.7	16.2				Very low	4	20	MV	24	Burlington Northern Santa Fe()	Average	869-3863	NY	212-392-2550
.0	10.2	8.1	7.3	10.0	7.8		Average	7	28	LG	5	Nokia Cl A(1)	High	869-3863	NY	212-392-2550
.8	8.4	13.1	10.4	11.3	8.0		High	6	20	LB	15	Philip Morris(3)	Low	523-4640	PA	215-988-1333
.0	11.6	15.0	12.0	12.3	8.9		High	2	19	LV	15	JC Penney(2)	Low	523-4640	PA	215-988-1333
.0	12.5	15.2	12.2				Average	2	19	LV	18	DuPont(3)	Low	523-4640	PA	215-988-1333
.2	8.8	14.8	13.3				Low	5	29	MG	37	Bay Networks(3)	High	523-4640	PA	215-988-1333
.2	13.6	27.4	25.0	16.6	14.3		Average	5	28	SG	23	Central Sprinkler(3)	High	523-4640	PA	215-988-1333
.9	10.1	18.8	17.6				Very low	16	18	SV	15	FNMA(3)	Low	523-4640	PA	215-988-1333
.2	12.1						Very low	11	22	LB	23	Hewlett-Packard(4)		748-8500		
.9	13.0	15.1	13.4	13.6	11.1		Low	5	19	LV	15	Digital Equipment(2)	Very low	621-3979		
.4	16.6	17.4	15.8	15.0	13.0		Very low	7	19	LV	26	General Motors(3)	Average	621-3979		
.0	3.7	11.2	8.0	10.8	6.9		Low	4	21	LB	28	Texaco(4)	Average	645-6561	MA	718-895-1206
.9	12.2	15.7	15.1	13.8	12.4		Very low	2	20	LG	27	Coca-Cola(6)	Average	645-6561	MA	718-895-1206
.0	11.1						Average	1	19	LB	12	Olin(2)		645-6561	MA	718-895-1206
.6	0.7	–0.4	–1.5	7.6	5.9		Average	18	41	MG	–35	Placer Dome(4)	High	554-4611	MA	718-895-1396
.6	13.5	15.2	12.4	12.3	8.5		Average	3	18	LV	23	IBM(3)	Average	645-6561	MA	718-895-1206
.1	8.1	7.6	7.6				High	0	22	LG	28	Hutchison Whampoa(3)	Low	645-6561	MA	718-895-1206
.0	10.8						High	6	21	LB	11	DuPont(3)		645-6561	MA	718-895-1206
.0	1.6	12.2	8.7	10.7	7.0		Very high	2	21	LB	14	BBC Brown Boveri (Reg)(3)	High	645-6561	MA	718-895-1206
r fund, not rated							Average	6	26	LV	2	Lucas Industries(2)		645-6561	MA	718-895-1206
.4	10.6						Low	9	22	MB	17	First Bank System(1)		645-6561	MA	718-895-1206
.9	12.2	19.3	16.5	13.9	12.1		High	5	23	SB	22	Integrated Silicon Solution(2)	Average	645-6561	MA	718-895-1206
.7	12.5	16.1	14.4				Low	6	20	LB	22	General Electric(2)	Average	645-6561	MA	718-895-1206
.8	6.8	13.2	11.1	11.6	8.4		High	3	21	LG	25	EMC(3)	Average	645-6561	MA	718-895-1206
.1	7.5	15.9	13.8				High	5	17	SV	18	Arrow Electronics(2)	Average	872-2710	GA	770-631-0414
.7	7.2	16.6	15.7				Average	8	28	LG	34	Nokia Cl A (ADR)(5)	High	432-4320	GA	404-396-8118
.3	13.7	18.3	16.1	14.7	11.5		Average	3	25	LG	37	Cisco Systems(5)	Average	432-4320	GA	404-396-8118
.7	14.6	13.4	12.5	15.5	13.8		Very low	14	22	LB	17	ANZ Banking Group(1)	Average	421-4120	CA	213-486-9200
r fund, not rated							Low	4	18	LB	–3	Jardine Matheson Holdings(3)		225-6265	MA	617-482-8260
.4	4.9	12.1	10.1	11.1	8.4		High	7	23	LB	19	American International Group(4)	Average	225-6265	MA	617-482-8260
.3	9.7	12.8	10.1	11.0	7.5		Low	3	19	LB	27	Astra Cl A Free(3)	Very low	225-6265	MA	617-482-8260
.9	6.5	11.5	8.1	11.7	7.9		Average	5	19	LV	26	Eastman Kodak(3)	Average	225-6265	MA	617-482-8260
.0	4.7	10.1	7.2	10.3	7.0		High	7	16	MV	15	Frontier(5)	Average	225-6265	MA	617-482-8260
r fund, not rated							Low	3	17	LV	17	Avnet(1)		807-2940		
r fund, not rated								2	18	LV	7	GTE(4)		807-2940		
.6	11.4	14.7	12.4	13.2	11.1		Average	12	17	LV	17	American General(4)	Low	807-2940		
.5	12.8	18.7	17.3	13.4	11.8		Low	4	24	LB	30	Mellon Bank(3)	Average	446-1012	MA	617-451-1912
.1	12.8	17.7	16.4				Average	4	24	MB	17	John Wiley(3)	Very low	446-1012	MA	617-451-1912
.6	7.9	18.8	17.8				Very low	7	20	SV	19	Conmed(9)	Low	932-3271	NY	518-234-7400
.6	6.7	14.1	11.7	13.9	11.3		Average	5	22	MB	39	USA Waste Services(2)	Average	245-5051	PA	412-288-1561
.3	10.6						Low	12	23	SB	13	Altera()		245-5040	PA	412-288-1900
.0	10.3	7.3	6.2	10.8	8.0		Average	1	27	LG	13	BBC Brown Boveri (Br)(2)	High	245-5051	PA	412-288-1561
.9	13.0	17.0	14.6	12.2	9.7		Low	2	17	LV	36	Hewlett-Packard(3)	Average	245-5040	PA	412-288-1900
.3	14.1	16.8	14.0	14.1	10.7		High	5	21	LB	16	Philip Morris(2)	Low	544-8888		
.6	15.4						High	11	24	LG	23	Intel(5)		522-7297	MA	617-439-6793
.6	17.6						High	15	18	LV	12	Philip Morris(4)		522-7297	MA	617-439-6793
.1	19.2	17.6	15.9				High	4	21	MB	10	Alcan Aluminium(1)	High	522-7297	MA	617-439-6793
.7	17.4	22.4	20.6				Average	15	19	LV	16	FNMA(5)	Low	522-7297	MA	617-439-6793
.0	7.7	13.7	11.9				Very high	1	23	MV	2	Union Camp(1)	Very low	522-7297	MA	617-439-6793
.3	16.1	9.8	9.5				Average	10	26	LV	8	Deutsche Bank(1)	High	522-7297	MA	617-439-6793
.6	13.8	16.5	13.9				High	0	18	MG	21	i-STAT(7)	Low	522-7297	MA	617-439-6793
.8	9.3	13.7	12.0				High	21	22	LB	8	FNMA(1)	Very low	544-8888		
.0	11.1						High	2	23	LB	8	IBM(2)		544-8888		
.9	8.3						High	38	22	LB	4	Philip Morris(1)		544-8888		
.1	7.3	12.2	10.0				Very high	1	13	MV	–1	Jefferson Smurfit(1)	Very low	544-8888		
.6	17.8	23.6	21.6				Very high	10	19	MB	14	General Motors(4)	Average	544-8888		
.7	9.6	8.5	8.1				Average	1	25	MB	4	Barrick Gold (Canada)(6)	High	544-8888		
.6	14.7	15.8	12.5				Average	7	20	MV	14	Centerior Energy(7)	Low	544-8888		
.8	16.1	24.1	22.1	19.4	17.4		Very high	10	22	MB	24	IBM(3)	Average	544-8888		
.8	17.8	23.7	19.4	18.1	13.9		Average	5	20	LV	32	FNMA(6)	Low	752-2347	MA	617-439-0547
.7	18.7	24.1	20.5	22.6	19.5		Average	8	19	LV	26	FNMA(5)	Average	752-2347	MA	617-439-0547
.8	12.5	18.5	16.0				Very high	11	22	LB	20	Coca-Cola(3)	Average	544-8888		
.7	16.6						High	8	24	LV	18	Hitachi(2)		544-8888		

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG. 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WITH OBJECTIVE
FIDELITY DIVIDEND GROWTH		Growth	528.8	416	No load	1.19	37.5	34.8	0.5	52/229
FIDELITY EMERGING GROWTH		Maximum growth	1249.9	97	3.75*	1.02	35.9	34.6	0.0	17/34
FIDELITY EMERGING MARKETS		Emerging markets	1085.6	-28	4.50*	1.52	-3.2	-3.7	1.8	3/7
FIDELITY EQUITY-INCOME		Equity-income	10492.1	42	2.00	0.69	31.8	29.6	2.4	12/34
FIDELITY EQUITY-INCOME II		Equity-income	11977.0	56	No load	0.81	26.4	24.9	1.7	24/34
FIDELITY EUROPE		Europe	500.9	5	4.00*	1.35	18.8	1.75	0.5	6/11
FIDELITY EUROPE CAPITAL APPREC.		Europe	180.7	-38	4.00*	1.54	14.7	14.0	1.9	9/11
FIDELITY EXPORT		Growth	382.0	381	3.00	1.22	32.2	29.9	0.0	123/229
FIDELITY FIFTY		Maximum growth	156.3	158	3.00	1.19	32.2	28.6	0.9	24/34
FIDELITY GLOBAL BALANCED		Multi-asset global	121.4	-49	No load	1.33	11.5	11.4	0.4	16/18
FIDELITY GROWTH & INCOME		Growth/income	14818.6	59	3.00	0.77	35.4	33.4	1.7	40/138
FIDELITY GROWTH COMPANY	AVG	Growth	6278.8	110	3.00	1.05	39.6	37.8	0.4	27/229
FIDELITY INTL. GROWTH & INCOME		Foreign	941.6	-26	No load	1.21	12.2	11.1	3.3	19/66
FIDELITY JAPAN		Pacific	378.0	-3	4.00*	1.42	-2.1	-2.1	0.0	19/22
FIDELITY LATIN AMERICA		Foreign	473.8	-23	4.50*	1.48	-16.5	-16.8	1.2	62/66
FIDELITY LOW-PRICED STOCK		Small company	3349.9	42	4.50*	1.11	24.9	22.2	1.2	70/99
FIDELITY MAGELLAN		Growth	53702.3	47	3.00	0.96	36.8	34.6	0.7	56/229
FIDELITY MARKET INDEX		Growth/income	689.0	125	0.50*	0.45	37.0	35.8	2.1	15/138
FIDELITY MID-CAP STOCK		Growth	1160.2	820	No load	1.22	33.9	31.8	0.4	103/229
FIDELITY NEW MILLENNIUM		Growth	594.2	86	3.00	1.29	52.1	48.9	0.0	2/229
FIDELITY OTC	AVG	Growth	2350.1	70	3.00	0.81	38.2	36.0	0.1	41/229
FIDELITY OVERSEAS		Foreign	2409.9	10	No load	1.24	9.1	8.3	1.2	37/66
FIDELITY PACIFIC BASIN		Pacific	469.2	-1	4.00*	1.54	-6.1	-6.1	0.0	21/22
FIDELITY PURITAN		Balanced	15628.3	33	2.00	0.77	21.5	19.6	2.8	51/57
FIDELITY REAL ESTATE INVESTMENT	AVG	Real estate	708.7	28	No load	1.03	10.9	9.2	5.1	2/3
FIDELITY RETIREMENT GROWTH		Growth	4071.6	28	No load	1.07	24.3	20.9	1.8	206/229
FIDELITY SELECT AIR TRANSPORT		Specialty	94.2	NM	3.75*	2.50	59.5	58.5	0.0	1/3
FIDELITY SELECT AMERICAN GOLD		Precious metals	313.6	0	3.75*	1.41	11.2	11.2	0.0	4/15
FIDELITY SELECT BIOTECHNOLOGY		Health care	846.5	114	3.75*	1.59	49.1	49.0	0.2	3/9
FIDELITY SELECT COMPUTERS		Technology	499.1	185	3.75*	1.69	51.7	46.3	0.0	4/14
FIDELITY SELECT DEVELOPING COMM.	AVG	Communications	296.0	7	3.75*	1.56	17.4	10.1	0.0	3/
FIDELITY SELECT ELECTRONICS		Technology	892.3	470	3.75*	1.71	69.4	61.4	0.0	1/14
FIDELITY SELECT ENERGY		Natural resources	131.5	36	3.75*	1.85	21.4	20.5	0.6	7/1
FIDELITY SELECT ENERGY SERVICE		Natural resources	254.1	400	3.75*	1.79	40.9	39.6	0.3	1/1
FIDELITY SELECT FINANCIAL SVCS.		Financial	251.1	167	3.75*	1.54	47.4	46.5	0.6	4/
FIDELITY SELECT FOOD & AGRICULTURE		Specialty	240.1	181	3.75*	1.68	37.5	35.0	0.5	2/
FIDELITY SELECT HEALTH CARE		Health care	1448.7	82	3.75*	1.36	45.9	43.7	0.6	6/
FIDELITY SELECT HOME FINANCE		Financial	586.9	351	3.75*	1.45	53.5	52.3	0.6	1/
FIDELITY SELECT INDUSTL. MATERIAL		Natural resources	112.4	-38	3.75*	1.53	15.4	15.2	0.6	10/1
FIDELITY SELECT MEDICAL DELIVERY		Health care	203.3	-18	3.75*	1.45	32.2	29.8	0.0	9/
FIDELITY SELECT PRECIOUS METALS		Precious metals	309.6	-32	3.75*	1.46	-3.3	-3.4	0.4	12/1
FIDELITY SELECT REGIONAL BANKS		Financial	322.3	197	3.75*	1.56	46.8	45.1	1.1	5/
FIDELITY SELECT SOFTWARE & COMP.	AVG	Technology	351.1	66	3.75*	1.50	46.1	41.4	0.0	6/1
FIDELITY SELECT TECHNOLOGY	AVG	Technology	400.6	76	3.75*	1.56	43.7	38.1	0.0	10/1
FIDELITY SELECT TELECOMMUN.		Communications	451.6	24	3.75*	1.55	29.7	27.2	0.8	2/
FIDELITY SELECT UTILITIES GROWTH	AVG	Utilities	312.6	54	3.75*	1.42	34.4	33.6	1.9	3/2
FIDELITY SMALL CAP STOCK		Small company	488.2	-27	3.00	0.90	26.6	24.3	0.6	65/9
FIDELITY SOUTHEAST ASIA		Pacific	664.5	1	4.50*	1.47	12.2	11.6	1.6	2/2
FIDELITY STOCK SELECTOR		Growth	1262.2	60	No load	1.09	36.5	32.9	0.8	58/22
FIDELITY TREND		Growth	1274.6	7	No load	0.89	22.1	16.8	0.6	217/22
FIDELITY UTILITIES		Utilities	1510.7	40	No load	0.87	30.6	28.7	3.3	11/2
FIDELITY VALUE		Growth	5745.8	54	No load	1.08	27.1	25.6	0.9	185/22
FIDELITY WORLDWIDE		World	654.1	-7	No load	1.32	7.2	6.8	1.1	36/4
59 WALL ST. EUROPEAN EQUITY		Europe	115.8	4	No load	1.37	16.5	15.4	0.0	8/1
59 WALL ST. PACIFIC BASIN EQUITY		Pacific	114.3	-5	No load	1.29	3.5	2.1	4.5	12/
FIRST EAGLE FUND OF AMERICA		Growth	136.2	30	No load	1.90	36.4	35.6	0.0	59/2
FIRST INVESTORS BLUE CHIP A		Growth/income	170.2	54	6.25	1.54†	34.0	32.3	1.1	50/1
FIRST INVESTORS GLOBAL A		World	228.3	10	6.25	1.84†	17.8	16.3	0.5	15/
FIRST INVESTORS SPECIAL SITUATION A		Small company	125.4	47	6.25	1.65†	23.9	22.7	0.0	72/
FIRST INVESTORS UTILITIES INCOME A		Utilities	91.8	49	6.25	0.70†	32.2	30.7	3.7	7/
FIRST OMAHA EQUITY		Growth	206.4	42	No load	1.04	26.9	24.2	2.2	186/2
FIRST PRIORITY EQUITY INVESTMENT		Growth/income	150.4	NM	2.00	1.10†	24.5	22.3	1.6	129/1
FLAG INVESTORS TELEPHONE INC. A	AVG	Communications	492.4	13	4.50	0.92†	33.8	30.3	2.7	1
FLAG INVESTORS VALUE BUILDER A		Balanced	183.8	35	4.50	1.35†	32.8	30.8	2.6	3/
FLEX-FUNDS MUIRFIELD		Asset allocation	93.9	15	No load	1.22†	26.0	20.8	0.9	14/
FORTIS ADVANTAGE ASSET ALLOC. A	AVG	Asset allocation	135.2	16	4.50	1.57†	22.0	20.2	3.0	24/
FORTIS ADVANTAGE CAPITAL APPR. A		Small company	95.0	38	4.50	1.69†	36.3	36.1	0.0	30/
FORTIS CAPITAL A		Growth	277.5	17	4.75	1.24†	21.6	21.4	0.4	219/2
FORTIS GROWTH A		Growth	640.2	17	4.75	1.13†	25.5	23.6	0.0	198/2
FORTRESS UTILITY		Utilities	801.7	4	2.00*	1.14	25.5	24.0	3.9	18/

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not mea

AGE ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE	
1 YEARS AFTERTAX	5 YEARS PRETAX	5 YEARS AFTERTAX	10 YEARS PRETAX	10 YEARS AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE
d, not rated						High	7	22	MB	13	Philip Morris(3)		544-8888	
15.1	24.1	22.3				Very high	9	31	MG	31	Oracle(5)	High	544-8888	
12.8	10.3	9.9				High	1	20	MG	–11	Telefonos de Mexico L (ADR)(3)	Very high	544-8888	
14.8	18.9	17.0	13.1	10.0		Average	6	18	LV	21	Philip Morris(3)	Low	544-8888	
13.8	22.0	20.2				Average	12	20	LV	12	American Express(4)	Low	544-8888	
16.4	10.3	9.6				Average	4	22	MB	29	Nokia Cl K(2)	High	544-8888	
d, not rated						Very high	9	17	MV	10	Fiat(3)		544-8888	
d, not rated						Very high	2	23	SB	13	TSX(4)		544-8888	
d, not rated						Very high	6	23	LB	12	Compaq Computer(2)		544-8888	
d, not rated						Very high	2	20	MV	–17	Jefferson Smurfit Group(2)		544-8888	
16.2	21.2	18.7	19.1	16.5		Average	9	22	LB	20	Philip Morris(4)	Low	544-8888	
14.7	20.5	18.5	17.0	14.7		High	10	24	LG	24	Intel(4)	Average	544-8888	
13.0	9.0	8.3				Very high	9	27	LV	9	Hitachi(4)	Average	544-8888	
10.5						High	4	36	MV	–11	Fuji Photo Film(4)		544-8888	
d, not rated						Average	7	21		–51	Grupo Carso Cl A1(4)		544-8888	
13.1	24.3	21.5				Average	22	15	SV	16	Lyondell Petrochemical(2)	Low	544-8888	
16.6	20.4	17.5	17.4	14.4		High	7	20	MB	31	Hewlett-Packard(2)	Average	544-8888	
14.0	16.2	15.3				Very low	0	20	LB	26	General Electric(2)	Average	544-8888	
d, not rated						High	11	25	MB	12	Digital Equipment(2)		544-8888	
22.7						Very high	10	29	MG	34	US Robotics(4)		544-8888	
11.3	20.1	17.5	15.7	13.2		Average	9	28	MG	26	Intel(6)	Average	544-8888	
15.0	8.3	6.9	13.4	11.1		Average	10	25	LV	13	CS Holdings (Br)(1)	High	544-8888	
12.9	9.2	8.3				High	2	35	MB	6	Nippon Shokubai(2)	Very high	544-8888	
11.7	16.6	13.8	13.0	9.8		Average	6	22	LV	11	Schlumberger(3)	Very low	544-8888	
6.8	16.2	14.6				Average	9	22	SV	2	Developers Diversified Rlty(5)	Average	544-8888	
11.7	19.6	15.9	15.2	11.4		Average	10	19	MV	16	IBM(3)	Low	544-8888	
16.5	19.0	17.9	11.1	10.1		Very high	4	14	MV	19	Northwest Airlines Cl A(9)	Very high	544-8888	
18.9	8.8	8.8	8.4	8.4		Low	5	44	SG	–6	Barrick Gold (Canada)(10)	Very high	544-8888	
7.1	17.0	15.7	16.8	15.9		Average	33	37	MG	14	Amgen(9)	Very high	544-8888	
30.6	30.3	28.6	16.4	15.5		Very high	11	22	MB	32	Micron Technology(9)	Very high	544-8888	
17.0	27.5	24.4				Very high	6	37	MG	21	DSC Communications(10)	High	544-8888	
33.8	35.2	32.8	12.8	11.8		Very high	0	24	MB	30	Micron Technology(9)	High	544-8888	
12.2	7.2	6.4	8.8	7.8		High	0	27	LB	6	Atlantic Richfield(8)	Very high	544-8888	
18.8	6.3	5.8	5.2	4.9		Very high	0	33	MG	6	Western Atlas(8)	Very high	544-8888	
15.8	31.0	28.5	14.1	12.5		High	16	13	LV	18	American Express(5)	High	544-8888	
14.4	17.7	15.5	19.1	17.3		High	6	23	LG	24	Ralcorp Holdings(10)	Low	544-8888	
20.4	22.4	19.9	20.5	18.6		High	22	27	LG	28	Schering-Plough(8)	High	544-8888	
23.3	39.1	37.1	21.0	18.7		High	13	14	SV	23	Standard Federal Bancorp(6)	Average	544-8888	
14.7	18.3	18.1				High	20	18	MB	2	ALCOA(10)	High	544-8888	
17.5	20.9	19.3				High	17	24	MB	40	Columbia/HCA Healthcare(8)	Very high	544-8888	
26.1	9.9	9.5	8.8	8.3		Average	5	39	SG	–15	Barrick Gold (Canada)(11)	Very high	544-8888	
14.4	32.1	29.1				High	20	12	LV	19	American Express(5)	Average	544-8888	
21.0	30.9	27.7	19.4	17.6		High	12	26	LG	34	Microsoft(10)	Very high	544-8888	
24.0	28.8	26.4	13.8	12.6		High	15	25	LG	37	Micron Technology(9)	High	544-8888	
18.2	21.5	19.8	19.4	18.2		High	8	25	LB	20	LM Ericsson Telephone (ADR)(8)	Average	544-8888	
9.6	13.4	11.0	13.1	11.3		Low	4	18	LV	13	Ameritech(8)	Low	544-8888	
d, not rated						Very high	12	24	SB	27	Grand Casinos(3)		544-8888	
d, not rated						High	4	20	LG	8	Hutchison Whampoa(4)		544-8888	
13.9	21.4	19.6				Very high	–2	22	LG	25	Oxford Health Plans(4)	Average	544-8888	
7.5	16.7	13.9	12.9	9.8		High	8	22	MB	29	Golden West Financial(4)	Average	544-8888	
10.5	14.0	11.8				High	2	18	LV	17	Ameritech(5)	Low	544-8888	
17.0	20.8	19.3	14.1	12.5		High	5	20	LV	15	Philip Morris(4)	Low	544-8888	
13.7	11.5	10.7				Average	22	20	MV	4	Deutsche Bank(2)	Average	544-8888	
10.7	10.8	9.2				High	2	20	MB	11	Guardian Royal Exchange(2)	High		MA 212-493-8100
10.0	11.4	9.5				Average	12	25	MB	–11	Public Finance(3)	Very high		MA 212-493-8100
15.2	19.9	17.2				Average	3	16	MV	29	Tejas Gas(6)	Average	451-3623	NY 212-943-9200
9.7	13.7	12.2				Average	5	21	LB	23	AT&T(4)	Average	423-4026	NY 212-858-8000
10.9	9.2	8.6	15.2	13.8		Average	4	23	LB	17	Tele Danmark Cl B (ADR)(3)	High	423-4026	NY 212-858-8000
11.5	20.5	19.1				Average	15	25	SG	19	US Office Products(2)	High	423-4026	NY 212-858-8000
d, not rated							4	17	LV	3	GTE(3)		423-4026	NY 212-858-8000
12.9						Very low	15	23	LB	16	Hewlett-Packard(5)		662-4203	
7.1						Average	4	21	LB	8	Merck(4)		433-2829	
11.9	15.4	13.6	15.7	12.9		Low	2	23	LB	37	SBC Communications(8)	Average	767-3524	
12.6						Low	1	17	LV	21	McDonnell Douglas(3)		767-3524	
7.7	14.3	11.0				Very high	0	23	MB	18	Fidelity Equity Growth Fund(11)	Very low	325-3539	OH 614-766-7000
8.8	13.1	11.6				High	1	27	LG	23	3Com(2)	Low	800-2638	MN 612-738-4000
12.8	20.9	20.4				Low	2	36	MG	45	Input/Output(4)	Very high	800-2638	MN 612-738-4000
7.2	15.3	13.9	12.9	10.7		Very low	5	26	LG	41	Silicon Graphics(5)	Average	800-2638	MN 612-738-4000
7.0	16.6	15.2	14.0	12.2		Low	9	33	MG	50	3Com(6)	Very high	800-2638	MN 612-738-4000
8.4	12.8	11.0				Average	3	15	MV	6	AT&T(4)	Low	245-5051	PA 412-288-1561

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL	% CHG. 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WITH OBJECTIV
FOUNDERS BALANCED	▲▲	Balanced	130.3	36	No load	1.26†	29.4	24.4	2.6	7/57
FOUNDERS BLUE CHIP	AVG	Growth/income	373.2	20	No load	1.21†	29.1	23.3	1.1	106/138
FOUNDERS DISCOVERY	▼	Small company	218.2	16	No load	1.67†	31.3	25.2	0.0	46/99
FOUNDERS FRONTIER	▼	Small company	332.1	33	No load	1.62†	37.0	31.6	0.0	27/99
FOUNDERS GROWTH	AVG	Growth	651.8	110	No load	1.33†	45.6	40.4	0.1	9/229
FOUNDERS SPECIAL	▼	Maximum growth	388.2	29	No load	1.36†	25.7	18.7	0.0	30/34
FOUNDERS WORLDWIDE GROWTH	▼	World	227.9	117	No load	1.66†	20.6	19.4	0.4	9/41
FOUNTAIN SQUARE INTERNATIONAL EQUITY		Foreign	92.5	116	4.50	1.65†	11.3	11.3	0.0	27/66
FOUNTAIN SQUARE QUALITY GROWTH		Growth	105.1	80	4.50	1.00†	31.6	31.1	1.1	131/229
FPA CAPITAL	▲	Small company	353.0	84	6.50‡	0.95	38.4	37.2	0.5	25/99
FPA PARAMOUNT	AVG	Growth/income	575.1	17	6.50‡	0.89	12.7	10.0	1.8	137/138
FRANKLIN BALANCE SHEET INVMT.	▲▲▲	Small company	450.1	213	1.50	1.19†	30.0	28.2	1.2	51/99
FRANKLIN DYNATECH	▼	Technology	91.0	31	4.50	1.01†	26.1	25.1	1.0	13/14
FRANKLIN EQUITY I	▼	Growth	345.5	27	4.50	0.95†	32.9	30.4	0.9	114/229
FRANKLIN EQUITY INCOME I	▲▲	Equity-income	190.6	101	4.50	0.77†	25.7	23.4	3.9	28/34
FRANKLIN GLOBAL UTILITIES I		Utilities	127.8	8	4.50	1.12†	27.5	25.6	2.8	15/26
FRANKLIN GOLD I	▼▼▼	Precious metals	355.6	–13	4.50	0.95†	–1.3	–2.8	1.7	8/15
FRANKLIN GROWTH I	AVG	Growth	803.3	49	4.50	0.90†	38.4	37.8	0.8	38/229
FRANKLIN INCOME I	▲▲▲	Balanced	6216.8	30	4.25	0.71†	21.3	18.1	7.7	53/57
FRANKLIN RISING DIVIDENDS I	AVG	Growth/income	273.8	14	4.50	1.43†	30.2	29.5	1.8	92/138
FRANKLIN SMALL CAP GROWTH I		Small company	245.7	516	4.50	0.69†	42.2	39.2	0.1	21/99
FRANKLIN UTILITIES I	▼	Utilities	2904.1	14	4.25	0.73†	30.7	28.5	5.0	9/26
FREMONT GLOBAL	▲	Multi-asset global	502.5	15	No load	0.88	19.3	16.8	3.3	11/18
FUNDAMENTAL INVESTORS	▲▲	Growth/income	4754.5	82	5.75	0.68†	34.2	32.4	1.7	49/138
G.T. GLOBAL AMERICA GROWTH A	▼	Growth	390.3	95	4.75	1.58†	23.2	18.8	1.0	212/229
G.T. GLOBAL EMERGING MARKETS A		Emerging markets	248.2	–26	4.75	2.06†	–13.9	–13.9	0.0	7/7
G.T. GLOBAL EUROPE GROWTH A	▼▼▼	Europe	470.4	–27	4.75	1.73†	9.9	9.4	0.9	11/11
G.T. GLOBAL GROWTH & INCOME B		World	370.8	5	5.00**	2.32†	14.6	13.3	2.9	23/4
G.T. GLOBAL HEALTH CARE A	▼▼	Health care	522.6	35	4.75	1.98†	37.0	32.4	0.0	8/
G.T. GLOBAL INTL. GROWTH A	▼▼▼	Foreign	294.1	–32	4.75	1.70†	3.9	2.5	0.0	54/6
G.T. GLOBAL JAPAN GROWTH A	▼▼▼	Pacific	108.5	8	4.75	1.91†	1.9	–1.2	0.0	16/2
G.T. GLOBAL NEW PACIFIC GROWTH A	▼▼▼	Pacific	369.1	–9	4.75	1.81†	7.4	6.2	0.8	3/2
G.T. GLOBAL TELECOMMUN. A		Communications	1344.6	–9	4.75	1.80†	8.6	7.1	0.0	6/
G.T. GLOBAL WORLDWIDE GROWTH A	▼▼	World	146.1	–20	4.75	1.81†	11.2	10.4	0.0	30/4
G.T. LATIN AMERICA GROWTH A		Foreign	194.5	–31	4.75	2.04†	–21.3	–21.5	0.7	65/6
GABELLI ASSET	▲▲	Growth	1090.4	11	No load	1.28†	24.9	22.4	0.9	202/22
GABELLI GLOBAL TELECOMMUNICATIONS		Communications	122.8	–11	4.50	1.80†	16.2	15.6	0.6	5/
GABELLI GROWTH	AVG	Growth	526.4	9	No load	1.36†	32.7	27.1	0.2	118/22
GABELLI SMALL CAP GROWTH		Small company	228.6	17	4.50	1.54†	25.3	22.9	0.0	69/9
GABELLI VALUE	AVG	Growth	486.4	11	5.50	1.50†	22.6	19.3	0.4	214/22
GALAXY EQUITY GROWTH RET.	AVG	Growth	116.7	71	No load	0.98	36.1	34.6	0.8	66/22
GALAXY EQUITY INCOME RET.	▲	Equity-income	91.2	50	No load	1.11	33.0	31.0	1.8	8/3
GALAXY EQUITY VALUE RET.	▲	Growth	104.3	42	No load	1.08	27.8	24.6	1.5	172/22
GALAXY GROWTH & INCOME EQTY. RET. (q)		Growth/income	192.5	748	4.00	1.29†	29.3	26.6	1.9	102/13
GALAXY II LARGE COMPANY INDX. RET.	AVG	Growth/income	214.4	56	No load	0.40	37.1	35.6	2.0	12/13
GALAXY II SMALL COMPANY INDEX RET.	▲	Small company	276.0	20	No load	0.40	33.1	31.8	1.8	41/9
GALAXY SMALL CAP EQUITY RET. (r)		Small company	129.2	561	4.00	1.31†	31.4	29.0	0.0	45/9
GAM INTERNATIONAL A	AVG	Foreign	559.2	251	5.00	1.60	30.1	28.3	4.7	1/6
GATEWAY INDEX PLUS	▲▲	Growth/income	176.2	7	No load	1.21	11.0	10.5	1.5	138/13
GEORGE PUTNAM FUND OF BOSTON A	▲	Balanced	1182.6	30	5.75	0.91†	30.1	27.3	3.6	5/5
GINTEL	▼▼	Growth	96.7	10	No load	2.40	31.0	28.8	0.1	137/22
GLOBAL UTILITY B		Utilities	221.7	–10	5.00**	2.02†	22.5	20.6	2.6	24/2
GOLDMAN SACHS ASIA GROWTH		Pacific	168.6	27	5.50	1.90†	6.5	5.9	2.1	6/2
GOLDMAN SACHS CAPITAL GROWTH	AVG	Growth	884.1	2	5.50	1.38†	25.7	20.0	0.7	196/22
GOLDMAN SACHS GROWTH & INCOME		Growth/income	413.5	129	5.50	1.25†	33.5	31.8	1.5	52/13
GOLDMAN SACHS INTL. EQUITY		Foreign	303.2	0	5.50	1.73†	18.9	16.2	3.3	6/6
GOLDMAN SACHS SELECT EQUITY A		Growth/income	115.7	26	5.50	1.38†	35.2	34.1	0.8	43/13
GOLDMAN SACHS SMALL CAP EQUITY		Small company	235.8	–29	5.50	1.53†	8.6	8.6	0.0	99/9
GOVETT SMALLER COMPANIES A		Small company	518.8	581	4.95	1.95†	69.0	65.8	0.0	1/9
GRADISON-McDONALD ESTAB. VALUE	▲	Growth	337.8	30	No load	1.20†	26.4	24.5	1.6	190/21
GRADISON-McDONALD OPPORT. VALUE	▲	Small company	97.1	17	No load	1.37†	26.8	25.5	0.8	63/9
GROWTH FUND OF AMERICA	AVG	Growth	7891.2	50	5.75	0.75†	29.8	27.0	0.9	148/21
GUARDIAN PARK AVENUE	▲▲	Growth	976.5	52	4.50	0.84†	34.3	32.0	0.9	98/21
HANCOCK EMERGING GROWTH B	▼	Small company	411.5	42	5.00**	2.19†	42.1	42.1	0.0	22/
HANCOCK GLOBAL A (s)		World	95.0	2	5.00	1.98†	10.6	8.5	0.0	32/
HANCOCK GLOBAL TECHNOLOGY A (t)	▼	Technology	155.0	197	5.00	2.16†	46.5	44.0	0.0	5/
HANCOCK GROWTH & INCOME A	▼	Growth/income	129.6	16	5.75	1.31†	36.7	35.7	1.6	19/1
HANCOCK GROWTH A	▼▼	Growth	241.7	65	5.00	1.65†	27.2	26.0	0.0	182/2
HANCOCK REGIONAL BANK B (u)	▲▲▲	Financial	1453.0	205	5.00**	2.06†	47.6	46.7	1.2	3
HANCOCK SOVEREIGN ACHIEVERS B	▼	Growth	91.4	2	5.00**	2.10†	24.0	23.7	0.1	209/2

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not mea
(q) Formerly Shawmut Growth & Income Equity Invmt. (r) Formerly Shawmut Small Cap Equity Invmt. (s) Formerly John Hancock Freedom Global A. (t) Formerly John Hancock Freedo

GE ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
ARS	5 YEARS		10 YEARS		BW 10-YEAR	TURNOVER	%CASH	P-E	STYLE	UNTAXED	LARGEST HOLDING				
AFTERTAX	PRETAX	AFTERTAX	PRETAX	AFTERTAX	ANALYSIS			RATIO			COMPANY (% ASSETS)				IN-STATE
12.6	15.0	12.4	12.0	9.1		Very high	19	23	LB	15	Home Depot(4)	Very low	525-2440	CO	303-394-4404
9.9	13.7	9.9	13.0	8.4		Very high	20	23	LB	23	Home Depot(4)	Average	525-2440	CO	303-394-4404
8.3	20.2	18.6				Average	13	27	SG	31	OPTi(3)	High	525-2440	CO	303-394-4404
13.5	20.3	18.4				Average	18	31	MG	35	Cascade Communications(2)	High	525-2440	CO	303-394-4404
18.4	22.1	19.4	16.9	13.9		Very high	14	30	LG	29	Intel(4)	High	525-2440	CO	303-394-4404
7.5	19.7	16.2	15.8	12.1		Very high	24	29	MG	23	HFS(2)	High	525-2440	CO	303-394-4404
14.4	16.0	15.4				Average	20	23	MG	17	Nokia(2)	Average	525-2440	CO	303-394-4404
d, not rated							5	30	LB	4	Royal Dutch Petroleum (ADR)(2)		334-0483	PA	513-744-8888
8.8						Low	4	21	LB	14	General Electric(5)		334-0483	PA	513-744-8888
19.3	29.0	26.9	19.0	16.2		Very low	15	16	MV	39	Green Tree Financial(9)	High	982-4372	CA	310-473-0225
11.2	15.2	12.1	14.5	10.8		High	29	22	MV	10	TIG Holdings(6)	Low	982-4372	CA	310-473-0225
16.9	22.3	20.7				Low	18	21	SV	11	Total Petroleum N Amer (Can)(2)	Very low	342-5236	CA	415-312-2000
11.3	15.0	14.0	12.8	11.4		Very low	25	23	LG	45	Intel(14)	Average	342-5236	CA	415-312-2000
9.4	13.3	10.6	11.4	8.8		Average	6	21	LB	23	Intel(3)	Average	342-5236	CA	415-312-2000
11.6	16.5	14.2				Average	23	18	LV	8	Dun & Bradstreet(2)	Very low	342-5236	CA	415-312-2000
13.6						Low	10	16	LV	4	Southern(4)		342-5236	CA	415-312-2000
16.9	6.6	5.8	10.8	9.5		Very low	2	37	MG	15	Barrick Gold(12)	Very high	342-5236	CA	415-312-2000
14.5	14.8	14.0	14.2	13.2		Very low	5	23	LB	41	Computer Sciences(4)	Average	342-5236	CA	415-312-2000
8.4	17.6	14.3	12.2	8.4		Average	22	15	LV	5	Pacific Gas & Electric(1)	Very low	342-5236	CA	415-312-2000
5.4	12.3	11.7				Very low	12	17	MV	19	Philip Morris(3)	Low	342-5236	CA	415-312-2000
21.5						High	6	24	SB	15	Advanced Semiconductor Mtrls(3)		342-5236	CA	415-312-2000
6.9	11.8	9.8	11.1	8.7		Very low	10	15	LV	13	Southern(5)	Average	342-5236	CA	415-312-2000
9.7	11.3	9.9				Average	6	24	LG	12	AT&T(1)	Very low	548-4539	CA	415-768-9000
14.7	18.2	15.7	15.1	12.1		Low	8	19	LB	24	Intel(2)	Low	421-4120	CA	415-421-9360
12.3	19.4	16.8				High	30	20	SV	21	Michaels Stores(5)	High	824-1580	CA	415-392-6181
10.3						High	3	22	MB	–8	Iscor(3)		824-1580	CA	415-392-6181
9.5	4.2	3.9	9.4	8.1		High	5	16	MB	–20	Prosegur (Reg)(3)	Very high	824-1580	CA	415-392-6181
10.4						High	3	17	LB	9	Broken Hill Proprietary(2)		824-1580	CA	415-392-6181
10.1	14.0	12.7				Average	3	28	LG	31	Roche Holding (Gen)(3)	High	824-1580	CA	415-392-6181
7.3	6.5	5.6	12.2	11.2		High	–1	26	MB	11	Hosiden Electronics(3)	High	824-1580	CA	415-392-6181
11.8	2.0	1.3	14.2	12.1		Average	10	39	MB	8	Autobacs Seven(5)	Very high	824-1580	CA	415-392-6181
10.1	7.6	6.4	15.5	12.3		High	16	16	LB	8	HSBC Holdings (HK)(9)	Very high	824-1580	CA	415-392-6181
14.0						Average	–1	31	LG	10	Nokia Free(7)		824-1580	CA	415-392-6181
8.5	10.5	9.6				Average	2	22	LG	18	Merck(2)	High	824-1580	CA	415-392-6181
3.0						High	7	29		–38	Empresa Nacl de Elec (ADR)(3)		824-1580	CA	415-392-6181
13.3	15.6	14.1				Low	4	22	MB	32	Time Warner(3)	Low	422-3554	NY	914-921-5100
d, not rated						Very low	4	28	LB	7	LIN Broadcasting(5)		422-3554	NY	914-921-5100
9.3	14.9	12.5				Average	8	24	LG	36	First Data(3)	Average	422-3554	NY	914-921-5100
12.7						Low	2	23	SB	28	United Television(3)		422-3554	NY	914-921-5100
15.4	17.3	14.3				Average	10	23	MB	25	Media General Cl A(15)	Average	422-3554	NY	914-921-5100
12.1	14.8	14.1				Low	15	23	LB	27	Thermo Electron(3)	Average	628-0414		
11.7	13.8	12.4				Low	12	20	LB	20	Ford Motor(3)	Low	628-0414		
12.4	15.2	12.8				Average	14	16	LV	17	FNMA(3)	Low	628-0414		
d, not rated						Average	9	18	LV	12	Hubbell Cl A(2)		628-0414		
13.6	16.0	14.9				Very low	2	19	LB	28	General Electric(2)	Average	628-0414		
11.2	18.5	17.4				Very low	3	21	MB	28	Microsoft(1)	Average	628-0414		
d, not rated						Low	7	23	SB	18	Sterling Software(2)		628-0414		
24.1	20.1	17.6	19.0	14.5		High	6	22	LV	13	Sandoz (Reg)(4)	Average	426-4685	NY	212-407-4600
6.5	9.3	7.9	10.1	7.5		Very low	3	20	LB	12	General Electric(6)	Very low	354-6339	OH	513-248-2700
10.4	13.8	11.2	12.4	9.0		High	4	19	LV	14	J. P. Morgan(1)	Very low	225-1581	MA	617-292-1000
2.1	10.0	8.3	9.6	7.0		Average	22	18	MV	19	FNMA(15)	High	243-5808	CT	203-622-6400
9.4						Low	0	19	LV	15	AT&T(5)		225-1852		
d, not rated							9	21	MG	–1	Metropolitan Bank & Trust(6)		526-7384		
8.8	18.2	15.1				Average	16	18	MV	25	Georgia-Pacific(4)	Average	526-7384		
d, not rated						Average	11	17	MV	14	McDonnell Douglas(4)		526-7384		
9.0						Average	0	23	MB	15	Santen Pharmaceutical(4)		526-7384		
13.3						Average	3	17	LV	28	Philip Morris(3)		526-7384		
5.6						Average	4	18	SV	–11	Black Box(4)		526-7384		
49.3						Very high	7	37	SG	25	Integrated Silicon Systems(4)		225-2222	IL	708-684-6000
13.6	15.6	14.1	13.4	11.4		Low	29	17	MV	31	Sun Microsystems(3)	Low	869-5999	OH	513-579-5700
10.1	16.4	15.0	11.8	10.3		Low	30	18	SV	28	DAKA International(2)	Low	869-5999	OH	513-579-5700
12.4	16.7	15.2	14.9	12.7		Low	21	23	LB	36	Intel(3)	Average	421-4120	CA	415-421-9360
15.0	21.0	18.8	15.3	12.3		Average	8	19	LB	31	Philip Morris(3)	Average	221-3253		
16.1	22.8	22.7				Low	3	30	SG	41	Madge (NV)(2)	High	225-5291		
9.6						Average	0	27	LG	21	Coca-Cola(2)		225-5291		
25.6	24.4	21.7	12.7	10.8		Average	8	24	MG	31	Integrated Device Technology(5)	High	225-5291		
10.2	14.0	12.2	11.8	9.3		Very high	0	20	LB	21	Northrop Grumman(5)	Average	225-5291		
8.4	14.8	13.1	12.4	9.7		Average	1	28	LG	32	Paychex(3)	High	225-5291		
19.8	33.8	31.7	20.1	17.2		Very low	22	13	MV	19	Mercantile Bancorp(1)	Low	225-5291		
7.3	12.1	10.6				Average	2	21	LB	10	UNUM(3)	Average	225-5291		

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WIT OBJECTI
HANCOCK SOVEREIGN INVESTORS A		Growth/income	1280.3	17	5.00	1.16†	29.2	28.1	2.2	104/13
HANCOCK SPECIAL EQUITIES A		Small company	635.7	104	5.00	1.62†	50.4	49.6	0.0	8/9
HANCOCK SPECIAL OPPORTUNITIES B		Growth	149.2	15	5.00**	2.22†	33.3	33.3	0.0	110/22
HARBOR CAPITAL APPRECIATION	AVG	Growth	989.3	314	No load	0.81	37.8	37.2	0.1	49/22
HARBOR GROWTH		Growth	136.1	1	No load	0.93	38.2	33.8	0.0	40/22
HARBOR INTERNATIONAL		Foreign	3460.2	17	No load‡	1.10	16.1	15.4	1.5	10/6
HARBOR INTERNATIONAL GROWTH		Foreign	147.0	113	No load	1.32	24.3	23.9	1.0	2/6
HARBOR VALUE	AVG	Growth/income	91.7	61	No load	1.04	35.4	31.2	2.6	39/13
HEARTLAND VALUE		Small company	1190.9	251	No load‡	1.39†	32.4	29.8	0.4	43/9
HOMESTEAD VALUE		Growth/income	141.8	57	No load	1.15	33.8	31.9	2.1	51/13
HOTCHKIS & WILEY EQUITY-INCOME		Equity-income	162.4	52	No load	1.00	34.4	31.3	2.5	4/3
HOTCHKIS & WILEY INTERNATIONAL		Foreign	97.9	253	No load	1.00	19.9	18.8	2.1	4/6
IAI EMERGING GROWTH		Small company	608.7	92	No load	1.25†	49.6	48.7	0.0	11/9
IAI INTERNATIONAL		Foreign	142.1	–5	No load	1.72†	9.1	6.3	3.9	36/6
IAI MIDCAP GROWTH		Growth	114.4	35	No load	1.25†	26.1	23.9	0.0	194/22
IAI REGIONAL	AVG	Growth	577.5	12	No load	1.23†	32.6	28.5	0.8	119/22
IDEX		Growth	339.8	30	8.50	1.29	47.3	41.4	0.2	5/22
IDEX 3		Growth	169.5	24	8.50‡	1.25	48.6	40.9	0.1	4/22
IDEX II GROWTH A		Growth	500.1	25	5.50	1.76†	47.2	41.8	0.0	6/22
IDS BLUE CHIP ADVANTAGE A	AVG	Growth/income	225.7	54	5.00	0.89	36.5	33.3	1.4	25/13
IDS DISCOVERY A		Small company	670.4	4	5.00	0.99	18.1	11.0	0.7	93/9
IDS DIVERSIFIED EQUITY-INCOME A		Equity-income	1163.9	23	5.00	0.88	23.8	22.6	3.1	29/3
IDS EQUITY SELECT A (v)		Growth/income	680.8	17	5.00	0.71	28.1	25.1	0.8	114/13
IDS EQUITY VALUE B (w)		Growth/income	1519.0	27	5.00**	1.61†	26.9	25.4	1.6	121/13
IDS GLOBAL GROWTH A		World	673.4	5	5.00	1.38	6.3	5.5	2.0	37/4
IDS GROWTH A		Growth	1578.2	57	5.00	0.83	41.1	39.2	0.0	19/22
IDS INTERNATIONAL A		World	811.5	5	5.00	1.33	10.5	9.6	1.5	33/4
IDS MANAGED RETIREMENT A		Growth/income	2595.0	15	5.00	0.85	19.2	17.2	1.0	136/13
IDS MUTUAL A		Balanced	2701.8	–8	5.00	0.83	25.0	23.2	4.0	32/5
IDS NEW DIMENSIONS A	AVG	Growth	4865.9	9	5.00	0.90	35.6	34.0	0.8	75/22
IDS PROGRESSIVE A		Growth	347.1	25	5.00	0.99	22.2	20.1	1.6	216/22
IDS STOCK A	AVG	Growth/income	2082.6	–8	5.00	0.76	25.7	23.7	2.1	125/13
IDS STRATEGY AGGRESSIVE B (x)		Maximum growth	948.3	31	5.00**	1.80†	35.0	32.8	0.0	20/3
IDS UTILITIES INCOME A		Utilities	672.4	15	5.00	0.89	23.5	21.9	4.3	22/2
INCOME FUND OF AMERICA		Asset allocation	13777.5	31	5.75	0.65†	29.1	26.7	5.2	7/3
INTERNATIONAL EQUITY		Foreign	205.9	18	No load	0.90	11.6	7.4	2.2	24/6
INVESCO ADVISOR EQUITY C (y)		Growth/income	114.0	46	1.00**	2.25†	30.3	29.1	0.6	90/1
INVESCO ADVISOR FLEX C (z)		Asset allocation	398.5	63	1.00**	2.25†	27.3	26.4	2.1	10/
INVESCO ADVISOR MUTLIFLEX C (aa)		Multi-asset global	175.2	46	1.00**	2.49†	21.6	20.9	1.4	7/
INVESCO DYNAMICS		Maximum growth	624.8	84	No load	1.20†	37.6	32.8	0.2	11/
INVESCO EMERGING GROWTH		Small company	212.7	19	No load	1.49†	30.0	29.3	0.4	50/
INVESCO EUROPEAN		Europe	221.0	–10	No load	1.20	19.2	15.8	1.7	5/
INVESCO GROWTH		Growth	535.5	20	No load	1.06†	29.5	23.9	0.9	150/2
INVESCO INDUSTRIAL INCOME		Equity-income	4256.1	15	No load	0.94†	27.3	25.5	3.1	22/
INVESCO PACIFIC BASIN		Pacific	193.4	–23	No load	1.24	4.0	3.5	0.6	9/
INVESCO STRATEGIC ENERGY		Natural resources	98.5	110	No load	1.53	19.8	19.5	0.8	9/
INVESCO STRATEGIC FINCL. SERVICES		Financial	432.5	83	No load	1.26	39.8	37.0	1.4	6
INVESCO STRATEGIC GOLD		Precious metals	163.4	–26	No load	1.32	12.7	12.7	0.2	3/
INVESCO STRATEGIC HEALTH SCIENCE		Health care	1040.3	113	No load	1.15	58.9	55.7	0.0	2
INVESCO STRATEGIC LEISURE		Specialty	262.3	0	No load	1.29	15.8	11.5	0.3	3
INVESCO STRATEGIC TECHNOLOGY		Technology	576.0	86	No load	1.12	45.8	39.0	0.0	7/
INVESCO STRATEGIC UTILITIES		Utilities	150.2	23	No load	1.18	25.3	23.9	3.7	19/
INVESCO TOTAL RETURN		Asset allocation	768.3	162	No load	0.95	28.6	27.2	3.3	8/
INVESCO VALUE EQUITY		Growth/income	174.8	62	No load	0.97	30.6	29.2	1.9	86/1
INVESTMENT COMPANY OF AMERICA	AVG	Growth/income	25678.3	33	5.75	0.60†	30.6	28.3	2.2	85/1
IVY GROWTH A		Growth	275.7	25	5.75	1.38†	27.3	25.4	0.9	179/2
IVY INTERNATIONAL A		Foreign	472.1	113	5.75	1.58†	12.6	12.2	1.0	16/
JANUS		Growth	12466.2	33	No load	0.91	29.4	27.4	NA	151/2
JANUS BALANCED		Balanced	138.9	49	No load	1.35	27.3	24.4	NA	16/
JANUS ENTERPRISE		Growth	498.9	41	No load	1.25	27.3	24.8	NA	178/2
JANUS GROWTH & INCOME		Growth/income	632.4	39	No load	1.22	36.4	31.6	NA	28/1
JANUS MERCURY		Growth	1596.4	131	No load	1.33	33.0	28.4	NA	112/2
JANUS OVERSEAS		Foreign	129.4	98	No load	1.73	22.1	21.4	NA	3
JANUS TWENTY		Growth	3057.4	22	No load	0.99	36.2	29.4	NA	65/2
JANUS VENTURE		Small company	1790.4	20	No load‡	0.91	26.5	21.9	NA	66
JANUS WORLDWIDE		World	1975.5	28	No load	1.23	21.9	20.3	NA	5
JAPAN		Pacific	550.3	–6	No load	1.08	–9.1	–9.4	0.0	22
KAUFMANN		Maximum growth	3159.8	99	0.20*	2.29†	36.9	36.2	0.0	15
KEMPER BLUE CHIP A		Growth/income	159.2	12	5.75	1.48	31.7	28.4	1.3	71/
KEMPER GROWTH A		Growth	1711.2	12	5.75	1.09	31.9	28.1	0.2	127/

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not me
(v) Formerly IDS Equity Plus. (w) Formerly IDS Strategy Equity. (x) Formerly IDS Strategy Aggressive Equity.(y) Formerly EBI Equity.(z) Formerly EBI Flex.(aa) Formerly EBI MultiF

AGE ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
EARS AFTERTAX	5 YEARS PRETAX	5 YEARS AFTERTAX	10 YEARS PRETAX	10 YEARS AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE	
9.1	13.4	11.9	12.6	10.1		Average	6	20	LB	17	General Electric(5)	Low	225-5291		
22.3	34.6	34.0	17.1	16.4		Average	9	41	SG	35	America Online(4)	High	225-5291		
id, not rated						Average	6	23	LG	11	Motorola(3)		225-5291		
15.9	22.1	20.3				Average	3	28	LG	22	Hewlett-Packard(4)	High	422-1050	OH	419-247-2477
11.7	15.3	12.8				High	4	32	MG	34	Medtronic(2)	High	422-1050	OH	419-247-2477
20.3	16.6	15.9				Low	3	19	LV	25	Gencor (ADR)(3)	High	422-1050	OH	419-247-2477
id, not rated						Average	2	19	LG	7	Roche Holding (Gen)(6)		422-1050	OH	419-247-2477
10.5	14.0	11.3				High	4	19	LV	14	General Electric(3)	Average	422-1050	OH	419-247-2477
15.3	27.8	25.5	15.3	13.0		Low	21	17	SV	16	ICN Pharmaceuticals(3)	Low	432-7856	WI	414-347-7777
16.6	16.3	15.3				Very low	14	17	LV	21	Southwest Airlines(2)	Low	258-3030		
12.4	18.2	16.3				Average	4	16	LV	19	Ford Motor(4)	Average	346-7301	CA	213-362-8900
18.3	14.7	13.1				Low	5	16	LV	8	Hafslund Nycomed Cl B(3)	High	346-7301	CA	213-362-8900
18.8						Average	17	49	MG	36	Oxford Health Plans(3)		945-3863	MN	612-376-2600
13.2	10.8	9.1				Low	3	24	LV	8	Iberdrola(3)	High	945-3863	MN	612-376-2600
16.6						Average	9	27	MB	18	Alco Standard(5)		945-3863	MN	612-376-2600
10.5	15.3	12.7	15.3	11.5		High	6	21	MB	20	Deere(4)	Average	945-3863	MN	612-376-2600
10.0	18.1	15.9	17.2	14.1		Average	11	26	LG	41	Microsoft(5)	High	851-9777	FL	813-585-6565
9.8	18.6	15.0				Average	10	27	LG	46	Microsoft(5)	High	851-9777	FL	813-585-6565
10.1	17.5	16.0				Average	8	27	LG	40	First Data(4)	High	851-9777	FL	813-585-6565
13.0	16.5	14.1				High	7	23	LB	21	General Electric(5)	Average	328-8300	MN	612-671-3733
3.5	14.7	12.5	10.8	8.5		Very high	15	23	SB	24	Horizon/CMS Healthcare(3)	High	328-8300	MN	612-671-3733
12.7	16.8	14.8				High	8	19	LV	13	General Electric(2)	Very low	328-8300	MN	612-671-3733
8.1	14.6	12.2	13.2	10.1		Average	5	21	MB	30	Crown Cork & Seal(2)	Average	328-8300	MN	612-671-3733
10.5	15.6	13.4	13.2	10.4		Average	11	16	LV	13	Dow Chemical(2)	Low	328-8300	MN	612-671-3733
10.5	8.8	8.3				Low	12	23	MB	1	Douglas Holdings(2)	High	328-8300	MN	612-671-3733
13.9	20.2	17.1	16.2	11.7		Average	7	27	LG	40	Coca-Cola(3)	High	328-8300	MN	612-671-3733
11.4	8.5	7.6	11.2	9.2		Average	5	31	LB	8	Next(2)	High	328-8300	MN	612-671-3733
7.0	15.8	13.0	14.9	12.6		Average	7	24	LB	16	Cisco Systems(2)	Average	328-8300	MN	612-671-3733
9.0	13.6	10.8	12.4	8.8		Average	9	16	LV	13	Dow Chemical(1)	Very low	328-8300	MN	612-671-3733
13.0	18.9	17.3	17.2	14.2		Average	11	25	LG	36	Cisco Systems(3)	Average	328-8300	MN	612-671-3733
9.2	15.9	14.1	9.9	6.9		Average	17	19	SV	12	Hormel Foods(2)	Low	328-8300	MN	612-671-3733
9.5	14.2	11.1	13.9	10.0		Average	4	19	LB	18	First Chicago(2)	Low	328-8300	MN	612-671-3733
9.1	15.2	13.7	12.9	11.6		High	5	31	MG	35	Parametric Technology(3)	High	328-8300	MN	612-671-3733
8.5	12.9	10.5				Average	6	19	MV	6	Enron(3)	Low	328-8300	MN	612-671-3733
10.5	14.7	13.8	12.2	9.2		Low	9	17	LV	12	Eli Lilly(2)	Very low	421-4120	CA	415-421-9360
14.7	10.2	[illegible]	12.6	10.8		Low	4	27	LG	28	National Westminster Bank(2)	High	344-8332	NY	212-841-3841
10.7	15.6	[illegible]	12.3	9.3		Low	6	20	LB	23	Lockheed Martin(2)	Low	525-8085	CO	303-930-6300
10.8	14.5	12.[illegible]				Low	7	18	LV	19	NBD Bancorp(2)	Very low	525-8085	CO	303-930-6300
id, not rated						Average	3	20	SV	10	Duke Realty Investments(2)		525-8085	CO	303-930-6300
13.1	24.8	21.3	14.8	11.9		Very high	11	27	MG	23	Viacom Cl B(3)	High	525-8085	CO	303-930-6300
13.0						Very high	5	24	SG	10	Zions Bancorp(3)		525-8085	CO	303-930-6300
11.6	7.5	6.4				Average	3	18	LB	21	Roche Holding (Gen)(3)	High	525-8085	CO	303-930-6300
8.1	15.3	11.8	11.7	8.6		High	4	26	LG	24	Amgen(3)	Average	525-8085	CO	303-930-6300
10.3	16.1	13.8	14.5	11.1		Average	5	19	LB	15	IBM(2)	Low	525-8085	CO	303-930-6300
14.1	8.7	7.7	12.7	10.9		Average	12	35	LG	7	Seventy-Seven Bank(2)	Very high	525-8085	CO	303-930-6300
8.8	1.7	1.4	5.4	4.7		Very high	15	28	MB	4	Phillips Petroleum(5)	Very high	525-8085	CO	303-930-6300
12.4	28.0	25.1				Very high	3	17	MV	12	Chemical Banking(5)	Average	525-8085	CO	303-930-6300
12.0	3.6	3.6	3.7	3.5		Average	–4	39	SG	–14	Diamond Fields Res (Canada)(10)	Very high	525-8085	CO	303-930-6300
12.9	19.4	18.4	23.2	21.7		High	20	36	MG	27	Amgen(4)	Very high	525-8085	CO	303-930-6300
11.6	23.0	20.1	18.2	15.2		High	9	27	MG	5	CBS(3)	Average	525-8085	CO	303-930-6300
17.2	30.0	26.3	20.5	18.5		Very high	10	26	MG	17	General Motors Cl E(3)	High	525-8085	CO	303-930-6300
8.3	14.1	11.7				Very high	12	18	MV	6	Rochester Gas & Electric(4)	Low	525-8085	CO	303-930-6300
12.6	15.3	13.6				Low	9	19	LV	14	Ford Motor(1)	Very low	525-8085	CO	303-930-6300
12.4	16.4	14.2				Low	1	19	LB	20	Philip Morris(2)	Low	525-8085	CO	303-930-6300
11.4	14.6	12.8	14.1	11.5		Low	12	19	LB	30	Philip Morris(3)	Low	421-4120	CA	213-486-9200
9.3	13.8	10.8	11.7	8.6		Average	5	22	LB	18	Fluor(2)	Average	456-5111	FL	407-393-8900
19.4	15.2	14.5				Very low	6	19	LV	16	Forte(2)	High	456-5111	FL	407-393-8900
10.9	16.7	15.0	15.6	12.7		High	14	23	LB	21	First Data(5)	Low	525-8983		
10.3						Very high	7	22	LB	13	Prudential(4)		525-8983		
15.6						Very high	0	35	MG	24	HFS(8)		525-8983		
9.7						High	4	27	LG	16	American Express(6)		525-8983		
id, not rated						Very high	6	35	MG	12	HFS(4)		525-8983		
id, not rated						Very high	11	29	MB	12	Industriforvaltning B Free(3)		525-8983		
7.4	17.8	16.2	15.1	12.8		High	2	25	LG	15	Sun Microsystems(6)	High	525-8983		
10.4	18.2	15.7	17.1	14.3		High	3	29	SG	21	Paging Network(4)	Average	525-8983		
16.0						High	6	29	LG	16	Industriforvaltning B Free(5)		525-8983		
5.8	1.2	0.1	10.8	6.8		Average	1	44	MV	–9	Nichiei(6)	Very high	535-2726	MA	617-439-4640
20.5	28.6	28.2				Average	3	31	SG	32	Altera(3)	High	237-0132	NY	212-922-0123
7.1	13.0	11.3				High	9	24	LG	23	General Electric(3)	Average	621-1048	IL	312-781-1121
6.2	15.7	14.1	14.1	11.1		High	10	24	LG	28	Johnson & Johnson(2)	High	621-1048	IL	312-781-1121

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG. 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WIT OBJECTI
KEMPER INTERNATIONAL A	◆◆	Foreign	304.2	–14	5.75	1.54	13.0	12.4	1.1	14/6
KEMPER RETIREMENT I	AVG	Balanced	108.4	9	5.00‡	0.91	23.7	20.2	3.8	40/5
KEMPER RETIREMENT II	AVG	Balanced	174.5	7	5.00‡	0.90	23.5	20.2	4.3	41/5
KEMPER RETIREMENT III		Balanced	127.0	9	5.00‡	0.95	26.2	23.0	3.9	24/5
KEMPER RETIREMENT IV		Balanced	150.6	6	5.00	0.97	27.5	26.0	3.9	15/5
KEMPER SMALL CAP EQUITY A	◆	Small company	566.4	19	5.75	1.14	31.2	25.7	0.0	47/9
KEMPER TECHNOLOGY A	◆	Technology	881.0	33	5.75	0.89	42.9	36.8	0.0	12/1
KEMPER TOTAL RETURN A	◆	Balanced	1790.1	9	5.75	1.13	25.8	23.0	3.0	28/5
KEYSTONE AMER. HARTWELL EM. GR. A	◆◆◆	Small company	105.0	–19	5.75	1.78†	22.4	18.8	0.0	77/9
KEYSTONE BALANCED (K-1) (bb)	AVG	Balanced	1471.4	14	4.00**	1.77†	27.1	25.5	3.0	17/5
KEYSTONE FUND OF THE AMERICAS B		World	92.9	–29	5.00**	2.54†	9.1	8.1	2.9	35/4
KEYSTONE GLOBAL OPPORTUNITIES B (cc)		World	274.0	91	5.00**	2.56†	22.7	22.7	0.0	4/4
KEYSTONE GROWTH & INCOME (S-1) (dd)	◆	Growth/income	222.5	18	4.00**	1.75†	31.9	27.1	0.7	69/13
KEYSTONE INTERNATIONAL	◆◆	Foreign	134.9	–4	4.00**	2.54†	11.5	10.8	1.4	25/6
KEYSTONE MID-CAP GROWTH (S-3) (ee)	◆	Growth	298.9	28	4.00**	1.32†	35.9	28.6	0.0	69/22
KEYSTONE OMEGA A (ff)	◆	Maximum growth	135.1	36	5.75	1.41	36.9	34.1	0.0	14/3
KEYSTONE PRECIOUS METALS HLDG.	◆◆◆	Precious metals	188.7	–11	4.00**	2.33†	–1.4	–1.4	0.0	9/1
KEYSTONE SMALL CO GROWTH (S-4) (gg)	◆	Maximum growth	1988.1	62	4.00**	1.78†	36.3	32.5	0.0	16/3
KEYSTONE STRATEGIC GROWTH (K-2) (hh)	◆	Growth	520.8	23	4.00**	1.73†	28.5	24.6	0.2	161/22
LANDMARK BALANCED A	AVG	Balanced	246.1	8	4.75	1.02†	22.7	20.8	3.1	47/5
LANDMARK EQUITY A	◆	Growth	213.8	15	4.75	1.05†	27.5	25.9	1.2	175/22
LEGG MASON SPECIAL INVMNT. PRIM.	◆	Small company	713.4	23	No load	1.93†	22.5	21.8	0.1	76/9
LEGG MASON TOTAL RETURN PRIM.	◆	Growth/income	242.1	25	No load	1.93†	30.4	29.0	3.3	87/13
LEGG MASON VALUE PRIM.	AVG	Growth	1340.4	44	No load	1.81†	40.8	38.6	0.7	23/22
LEXINGTON CORPORATE LEADERS	AVG	Growth/income	255.6	63	No load	0.62	39.2	36.7	4.8	3/13
LEXINGTON GOLDFUND	◆◆◆	Precious metals	136.4	–14	No load	1.54†	–1.9	–1.9	0.2	11/1
LEXINGTON GROWTH & INCOME	AVG	Growth/income	138.8	12	No load	1.15†	22.6	18.8	1.3	134/13
LEXINGTON WORLDWIDE EMERGING	◆◆	Emerging markets	239.8	–28	No load	1.65	–5.9	–6.2	0.8	5
LIBERTY EQUITY-INCOME A	◆◆◆	Equity-income	182.9	82	5.50	1.00	33.9	32.0	3.0	6/
LIBERTY UTILITY A	◆	Utilities	817.4	12	5.50	1.10	25.5	24.0	3.8	17/
LINDNER DIVIDEND	◆◆◆	Balanced	2088.5	30	No load	0.61	21.5	18.8	6.7	50/
LINDNER GROWTH (ii)	◆	Growth	1407.9	–6	No load	0.54	19.9	17.3	4.1	224/2
LKCM SMALL CAP EQUITY		Small company	122.8	NM	No load	1.00	33.2	32.8	1.0	40/
LONGLEAF PARTNERS	◆◆◆	Growth	1876.5	149	No load‡	1.17	27.5	26.3	1.1	174/2
LONGLEAF PARTNERS SMALL-CAP	AVG	Small company	136.0	37	No load	1.38	18.6	15.8	0.8	91/
LORD ABBETT DEVELOPING GROWTH	◆	Small company	195.4	47	5.75	1.31†	45.7	37.5	0.0	17/
LORD ABBETT VALUE APPRECIATION	AVG	Growth	227.1	19	5.75	1.12†	26.1	22.0	1.2	193/2
MAINSTAY CAPITAL APPRECIATION B	◆	Growth	856.1	72	5.00**	1.80†	35.1	35.0	0.0	83/2
MAINSTAY EQUITY INDEX A	AVG	Growth/income	109.3	78	3.00	0.90†	35.7	34.6	1.4	35/1
MAINSTAY TOTAL RETURN B	AVG	Balanced	860.9	33	5.00**	1.70†	28.0	27.3	1.8	12/
MAINSTAY VALUE B	◆◆	Growth/income	708.8	50	5.00**	1.90†	28.0	27.0	1.0	115/1
MANAGERS INTERNATIONAL EQUITY	AVG	Foreign	140.1	62	No load	1.49	16.3	14.5	0.3	9/
MANAGERS SPECIAL EQUITY	◆◆	Small company	118.3	8	No load	1.37	33.9	29.5	0.0	36/
MANNING & NAPIER SMALL CAP		Small company	142.9	37	No load	1.10	14.6	8.3	0.0	96/
MARKETWATCH EQUITY		Growth/income	119.5	16	4.50	1.35†	34.6	33.6	1.4	47/1
MARQUIS GROWTH & INCOME A		Balanced	92.4	36	3.50	0.85	22.9	21.2	3.3	45/
MARSHALL EQUITY-INCOME		Equity-income	132.8	118	No load	1.01	34.2	32.5	2.8	5/
MARSHALL INTERNATIONAL STOCK		Foreign	102.4	NM	No load	1.54†	11.6	10.7	2.2	23/
MARSHALL MID-CAP STOCK		Growth	108.3	56	No load	1.01	33.8	31.1	0.0	105/2
MARSHALL STOCK		Growth/income	273.2	21	No load	0.98	33.2	31.0	0.8	56/1
MARSHALL VALUE EQUITY		Growth/income	204.7	5	No load	0.96	25.4	22.3	1.7	126/1
MASSACHUSETTS INVESTORS A	AVG	Growth/income	2074.4	35	5.75	0.71†	39.3	35.6	1.8	2/1
MASSACHUSETTS INVESTORS GR. STK. A	◆◆	Growth	1122.7	16	5.75	0.72†	28.3	23.6	0.0	166/2
MATHERS	◆	Asset allocation	232.3	–21	No load	0.93	7.0	5.3	5.2	33
MENTOR GROWTH B	◆	Growth	254.6	34	4.00**	2.01†	39.4	35.3	3.0	30/2
MENTOR STRATEGY B		Asset allocation	234.3	33	4.00**	2.08†	26.2	26.2	0.0	13
MERGER	◆◆◆	Growth	245.6	43	No load	1.58†	14.2	12.2	0.5	227/2
MERIDIAN	AVG	Small company	375.0	46	No load	1.06	21.8	21.0	0.5	78
MERRILL LYNCH BALANCED INV. & RET. D		Balanced	471.8	36	5.25	1.27†	19.3	17.0	2.8	55
MERRILL LYNCH BASIC VALUE B	◆	Growth/income	2894.6	59	4.00**	1.61†	31.6	30.1	1.8	75/
MERRILL LYNCH CAPITAL B	◆	Growth/income	4785.5	46	4.00**	1.59†	31.5	27.8	2.8	77/
MERRILL LYNCH DEVEL. CAPTL. MKTS. B		Emerging markets	197.2	56	4.00**	2.79†	–4.3	–4.6	1.1	7
MERRILL LYNCH DRAGON B		Pacific	991.3	8	4.00**	2.40†	6.7	6.6	0.3	52
MERRILL LYNCH EUROFUND B	◆◆	Europe	763.9	–20	4.00**	2.06†	12.4	9.8	0.9	101
MERRILL LYNCH FUND FOR TOMORROW D		Growth	224.6	42	5.25	1.43†	27.1	23.9	0.0	184/
MERRILL LYNCH GLOBAL ALLOC. B	◆◆◆	Multi-asset global	7100.7	15	4.00**	1.91†	23.1	20.2	5.2	58
MERRILL LYNCH GLOBAL RESOURCES D		Natural resources	109.6	85	5.25	1.39†	9.8	9.5	0.8	111
MERRILL LYNCH GLOBAL SMALLCAP B		World	111.7	–26	4.00**	NA†	4.9	3.1	0.6	39
MERRILL LYNCH GLOBAL UTILITY B	AVG	Utilities	394.6	–11	4.00**	1.63†	22.7	21.1	2.7	23
MERRILL LYNCH GROWTH INV. & RET. B	◆	Growth	2037.2	55	4.00**	1.84†	35.4	32.3	0.1	80/

*Includes redemption fee **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not me
(bb) Formerly Keystone Custodian K-1. (cc) Formerly Keystone America Global Opportunity B. (dd) Formerly Keystone Custodian S-1. (ee) Formerly Keystone Custodian S-3. (ff) Form
stone America Omega A. (gg) Formerly Keystone Custodian S-4. (hh) Formerly Keystone Custodian K-2. (ii) Formerly Lindner.

GE ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
ARS AFTERTAX	5 YEARS PRETAX	5 YEARS AFTERTAX	10 YEARS PRETAX	10 YEARS AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL FREE (800)	IN-STATE	
12.6	8.9	8.0	11.7	9.1		High	1	27	LB	14	Roche Holding(4)	High	621-1048	IL	312-781-1121
5.5	13.5	10.3				Average	4	24	LB	20	Wal-Mart Stores(1)	Low	621-1048	IL	312-781-1121
6.1	13.6	11.3				Average	2	24	LB	17	Home Depot(1)	Low	621-1048	IL	312-781-1121
7.8						Average	2	24	LB	18	Wal-Mart Stores(1)		621-1048	IL	312-781-1121
d, not rated						Average	3	24	LB	7	Wal-Mart Stores(1)		621-1048	IL	312-781-1121
11.2	20.2	17.3	14.0	10.8		High	7	31	SG	20	Wisconsin Central Transport(3)	High	621-1048	IL	312-781-1121
17.2	20.4	16.0	14.9	10.8		Average	0	29	LG	48	Hewlett-Packard(4)	High	621-1048	IL	312-781-1121
6.1	12.9	10.6	11.1	8.7		High	2	24	LG	19	Coca-Cola(2)	Average	621-1048	IL	312-781-1121
6.2	17.1	15.4	16.5	14.3		High	10	41	SG	30	McAfee Associates(5)	Very high	343-2898	MA	617-338-3400
8.3	11.4	9.5	10.8	8.1		High	1	20	LB	21	General Electric(4)	Low	343-2898	MA	617-338-3400
d, not rated						High	3	19	MB	–10	Telebras(3)		343-2898		
d, not rated						Low	6	28	SG	19	Adobe Systems(3)		343-2898	MA	617-338-3400
8.0	11.9	9.4	11.0	8.2		High	4	21	LB	19	General Electric(2)	Average	343-2898	MA	617-338-3400
9.5	9.8	8.7	9.1	7.4		High	12	25	LV	14	Canon(4)	Average	343-2898	MA	617-338-3400
8.4	16.0	12.8	12.3	8.9		Very high	7	31	MG	18	CUC International(3)	Average	343-2898	MA	617-338-3400
13.3	19.9	16.8	16.1	12.5		High	2	33	MG	20	Warner-Lambert(3)	High	343-2898	MA	617-338-3400
19.9	10.0	9.9	9.6	8.9		Average	0	37	SG	0	Euro-Nevada Mining(8)	Very high	343-2898	MA	617-338-3400
16.6	26.6	23.1	15.5	12.4		Average	3	29	MG	37	EMC(4)	Very high	343-2898	MA	617-338-3400
8.9	16.7	13.6	12.6	9.4		Average	3	24	LB	20	General Electric(2)	High	343-2898	MA	617-338-3400
8.0	12.5	11.5				Low	4	18	LB	12	General Electric(2)	Low		MA	212-559-7117
11.6	14.9	14.2				Low	7	19	LB	19	Royal Dutch Petroleum (ADR)(3)	Average		MA	212-559-7117
9.3	16.3	15.6	12.5	11.3		Low	5	19	SV	19	America Online(7)	High	577-8589	MD	410-539-0000
9.7	17.3	15.9	9.4	7.7		Average	8	18	LV	13	Lloyds Bank(4)	Average	577-8589	MD	410-539-0000
15.8	19.0	18.3	11.7	10.2		Low	6	16	LV	45	FNMA(7)	Average	577-8589	MD	410-539-0000
14.2	16.3	13.2	15.1	10.6			5	19	LV	45	Mobil(9)	Average	526-0056	NJ	201-845-7300
19.3	4.9	4.7	7.4	7.1		Low	4	39	MG	–10	Barrick Gold (Canada)(6)	Very high	526-0056	NJ	201-845-7300
7.1	13.5	10.2	10.4	6.7		Average	0	20	LV	12	Xerox(2)	Average	526-0056	NJ	201-845-7300
9.1	11.3	9.4	9.6	6.9		Average	2	18	MB	–17	HM Sampoerna(2)	High	526-0056	NJ	201-845-7300
14.2	19.3	17.4				High	4	18	LB	11	Lockheed Martin(3)	Very low	245-5051	PA	412-288-1561
7.9	12.8	10.7				Average	5	16	MV	11	Sonat(3)	Low	245-5051	PA	412-288-1561
7.7	15.8	12.9	12.1	8.5		Low	7	17	MV	4	Minorco (ADR)(2)	Very low		MD	314-727-5305
10.3	14.7	12.8	12.3	9.1		Low	13	23	SV	20	Acordia(3)	Low		MD	314-727-5305
d, not rated							8	28	SB	12	AMP(3)			TX	817-332-3235
17.5	23.3	21.2				Low	16	21	MB	19	Knight-Ridder(8)	Low	445-9469	TN	901-761-2474
12.3	14.7	13.8				Low	3	18	SV	15	White River(6)	Average	445-9469	TN	901-761-2474
16.2	21.4	18.3	11.4	9.3		Low	2	28	SG	46	Applied Materials(9)	High	874-3733	NY	212-848-1800
8.5	15.0	12.4	11.5	8.2		Average	5	17	MV	18	Moore(3)	Average	874-3733	NY	212-848-1800
14.5	23.2	21.8				Low	10	22	LB	30	Micron Technology(3)	High	522-4202		
12.7	15.1	14.5				Very low	11	20	LB	29	General Electric(2)	Average	522-4202		
10.5	14.4	13.2				Very high	0	22	LB	23	Micron Technology(2)	Average	522-4202		
11.9	19.6	17.6				Average	8	18	MV	15	Philip Morris(2)	Low	522-4202		
17.0	15.1	14.4	14.9	12.7		Low	8	24	LB	19	Veba(2)	Average	835-3879	CT	203-857-5321
13.0	21.8	19.2	16.1	13.1		Average	10	27	SG	27	FirstFed Michigan(2)	Average	835-3879	CT	203-857-5321
9.5						Low	5	26	SB	21	Westcott Communications(5)		466-3863		
d, not rated						Low	1	20	LB	19	Merck(2)		232-9091		
d, not rated						Average	6	16	LV	9	Textron(1)		462-9511		
d, not rated						Average	13	18	LV	13	General Electric(6)		236-8560	PA	414-287-8500
d, not rated							18	14	LV	1	Astra(2)		236-8560	PA	414-287-8500
d, not rated						High	7	23	MB	20	Harley-Davidson(3)		236-8560	PA	414-287-8500
8.2						Average	7	25	MB	18	Royal Dutch Petroleum(3)		236-8560	PA	414-287-8500
d, not rated						Average	12	19	LV	12	IBM(3)		236-8560	PA	414-287-8500
10.9	15.8	11.5	14.7	10.4		High	4	20	LB	31	Philip Morris(3)	Average	637-2929	MA	617-954-5000
7.1	16.6	13.3	13.2	9.3		Average	8	28	LG	41	Intel(7)	High	637-2929	MA	617-954-5000
–0.2	3.0	1.6	8.8	5.1		Very high	3	42	SG	–7	ICN Pharmaceuticals(5)	Low	962-3863	IL	708-295-7400
12.8	21.8	19.2	13.0	11.4		Average	13	26	SB	38	Vencor(3)	Average	825-5353	VA	804-649-2311
d, not rated						High	18	26	MG	16	Target Therapeutics(1)		825-5353	VA	804-649-2311
10.9	12.1	10.3				Very high	43	24	MB	8	LIN Broadcasting(8)	Very low	343-8959	NY	914-741-5600
10.7	20.4	19.2	14.5	12.4		Low	27	36	MG	17	Service International(4)	Average	446-6662	CA	415-461-6237
d, not rated							5	24	LB	12	Computer Sciences(2)		637-3863	NJ	609-282-2800
15.5	17.2	15.6				Very low	16	16	LV	25	Sears Roebuck(3)	Low	637-3863	NJ	609-282-2800
11.3	13.7	11.4				High	6	17	LV	15	YPF (ADR)(2)	Low	637-3863	NJ	609-282-2800
d, not rated							2	17	SB	–8	Korea Mobile Telecom(4)		637-3863	NJ	609-282-2800
17.8						Very low	7	19	LG	21	Hongkong Telecommunications(4)		637-3863	NJ	609-282-2800
12.8	10.3	8.9				Average	7	18	LB	14	Philips Electronics(5)	High	637-3863	NJ	609-282-2800
d, not rated							10	22	LB	23	Chrysler(5)		637-3863	NJ	609-282-2800
10.8	15.2	12.8				Average	13	19	LV	5	Republic New York(1)	Very low	637-3863	NJ	609-282-2800
d, not rated							2	25	MB	–9	Newcrest Mining(3)		637-3863	NJ	609-282-2800
d, not rated							6	23	SV		Ahrend Groep(2)		637-3863	NJ	609-282-2800
9.4	10.8	9.6				Low	3	16	LV	10	China Light & Power(3)	Low	637-3863	NJ	609-282-2800
19.0	19.2	17.1				Very low	21	29	MG	33	Cirrus Logic(9)	High	637-3863	NJ	609-282-2800

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL	% CHG 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK W OBJEC
MERRILL LYNCH HEALTHCARE B	♦♦♦	Health care	143.9	128	4.00**	2.85†	48.1	46.3	0.0	4
MERRILL LYNCH INTL. EQUITY B		Foreign	921.2	–12	4.00**	2.13†	4.6	4.6	0.0	52/
MERRILL LYNCH LATIN AMERICA B		Foreign	478.0	–36	4.00**	2.51†	–24.6	–24.6	0.0	66/
MERRILL LYNCH PACIFIC B	♦♦	Pacific	1041.8	14	4.00**	1.94†	7.2	6.5	0.5	4/
MERRILL LYNCH PHOENIX B	AVG	Small company	402.4	18	4.00**	2.34†	20.7	19.1	0.3	81/
MERRILL LYNCH SPECIAL VALUE B	♦♦	Small company	323.3	81	4.00**	2.20†	21.1	19.7	1.9	79/
MERRILL LYNCH STRATEGIC DIV. B	AVG	Equity-income	111.1	–18	4.00**	2.09†	30.7	26.2	1.9	14/
MERRILL LYNCH TECHNOLOGY B		Technology	637.0	4	4.00**	2.38†	4.8	3.1	0.0	14/
MFS CAPITAL GROWTH B	AVG	Growth	438.4	11	4.00**	2.18†	39.5	34.0	0.0	28/2
MFS EMERGING GROWTH B	♦	Small company	2055.4	156	4.00**	2.14†	40.1	40.1	0.0	23/
MFS GROWTH OPPORTUNITIES A	♦	Growth	719.3	22	5.75	0.86†	34.5	29.8	0.0	94/2
MFS MANAGED SECTORS A		Growth	197.6	78	5.75	1.46†	33.1	26.3	0.0	111/2
MFS RESEARCH A	♦	Growth	563.7	75	5.75	0.95†	38.6	36.2	0.3	33/2
MFS TOTAL RETURN A	♦♦	Balanced	2356.2	29	4.75	0.87†	26.9	23.7	4.2	21/
MFS VALUE A	♦♦	Growth	232.1	63	5.75	1.37†	44.2	40.6	0.0	12/2
MFS WORLD ASSET ALLOCATION B		Multi-asset global	95.0	59	4.00**	2.24†	20.6	18.5	1.9	8/
MFS WORLD EQUITY B	♦	World	159.2	–3	4.00**	2.58†	17.3	16.0	0.0	18/
MFS WORLD GROWTH B		World	252.8	10	4.00**	2.39†	15.4	12.7	0.0	20/
MFS WORLD TOTAL RETURN A	AVG	Multi-Asset Global	115.8	21	4.75	1.76†	20.3	18.6	4.6	9/
MONETTA	♦	Small company	362.7	–1	No load	1.35	28.0	22.2	0.1	60/
MONTGOMERY ASSET ALLOCATION		Asset allocation	120.8	NM	No load	1.31	32.6	30.9	1.4	3
MONTGOMERY EMERGING MARKETS		Emerging markets	855.1	–3	No load	1.80	–9.1	–9.1	0.0	
MONTGOMERY GLOBAL COMMUNICATIONS		Communications	220.0	2	No load	1.91	16.9	16.9	0.0	
MONTGOMERY GROWTH		Growth	859.8	45	No load	1.50	23.6	20.8	0.8	211/2
MONTGOMERY MICRO CAP		Small company	272.2	NM	No load‡	1.75	28.7	28.3	0.6	57
MONTGOMERY SMALL CAP	AVG	Small company	236.5	17	No load‡	1.37	35.1	31.8	0.0	33
MORGAN STANLEY ASIAN GROWTH A		Pacific	183.4	16	4.75	1.90†	6.4	6.4	0.0	7
MUTUAL BEACON	♦♦♦	Growth/income	3566.7	73	No load	0.75	25.9	22.9	4.9	124/
MUTUAL DISCOVERY		Small company	1368.3	89	No load	0.99	28.6	26.3	3.3	59
MUTUAL QUALIFIED	♦♦♦	Growth/income	2999.4	68	No load	0.73	26.6	22.3	4.0	123/
MUTUAL SHARES	♦♦♦	Growth/income	5224.9	40	No load	0.72	29.1	23.6	4.9	105/
NATIONS EQUITY-INCOME INV. N		Equity-income	100.8	78	5.00**	1.67†	26.7	24.7	2.5	23
NATIONWIDE	AVG	Growth/income	846.2	33	4.50	0.63	30.0	27.5	1.8	96/
NATIONWIDE GROWTH	AVG	Growth	604.5	37	4.50	0.68	28.7	24.8	1.5	157/
NAVELLIER AGGRESS SMALL CAP EQTY.		Small company	107.8	486	3.00	1.68	43.9	43.0	0.0	19
NEUBERGER & BERMAN FOCUS (jj)	AVG	Growth	1027.5	70	No load	0.87	36.2	34.3	0.4	64/
NEUBERGER & BERMAN GENESIS	♦	Small company	118.6	10	No load	1.35	27.3	25.3	0.0	62
NEUBERGER & BERMAN GUARDIAN	♦♦	Growth/income	4389.5	81	No load	0.80	32.1	30.5	1.2	67/
NEUBERGER & BERMAN MANHATTAN	♦	Growth	594.6	29	No load	0.98	31.0	28.3	0.0	136/
NEUBERGER & BERMAN PARTNERS	AVG	Growth	1656.9	33	No load	0.83	35.2	30.8	0.8	81/
NEW ECONOMY	AVG	Growth	3545.9	37	5.75	0.85†	24.4	22.5	1.1	205/
NEW ENGLAND BALANCED A	♦	Balanced	196.6	24	5.75	1.40†	26.3	23.6	2.9	23
NEW ENGLAND CAPITAL GROWTH A		Growth	123.5	29	5.75	1.63†	30.7	28.4	0.0	139/
NEW ENGLAND GROWTH A	♦♦	Growth	1201.6	22	6.50‡	1.19†	38.1	32.7	0.4	44/
NEW ENGLAND GROWTH OPPTY. A	AVG	Growth/income	150.6	45	5.75	1.28†	35.1	29.9	1.1	44/
NEW ENGLAND INTL EQUITY A		Foreign	137.1	–4	5.75	1.75†	6.0	5.4	1.6	4
NEW ENGLAND STAR ADVISERS A		Growth	223.6	145	5.75	1.94†	34.4	32.2	0.0	97
NEW ENGLAND VALUE A	AVG	Growth/income	241.3	26	5.75	1.37†	32.3	29.1	1.0	65
NEW PERSPECTIVE	♦	World	9292.3	42	5.75	0.83†	20.4	18.6	1.8	1
NEW USA MUTUAL		Growth	197.4	7	5.00	2.12†	43.1	37.6	0.0	13
NICHOLAS	♦	Growth	3505.3	24	No load	0.77	35.4	32.6	1.0	79
NICHOLAS II	♦	Small company	693.3	15	No load	0.66	28.6	25.5	0.9	58
NICHOLAS LIMITED EDITION	♦♦	Small company	169.6	19	No load	0.90	30.2	25.2	1.4	49
NICHOLAS-APPLEGATE CORE GRTH. C (kk)		Growth	169.9	27	1.00**	2.24†	36.8	36.8	0.0	55
NICHOLAS-APPLEGATE EMRG GRTH. C (ll)		Small company	192.0	33	2.00***	2.44†	34.2	34.0	0.0	39
NICHOLAS-APPLEGATE GROWTH EQTY. B		Maximum growth	291.0	13	5.00**	2.32†	30.1	28.9	0.0	23
NORTHERN GROWTH EQUITY		Growth	192.5	102	No load	1.00	26.1	25.7	0.7	192
NORTHERN INTL GROWTH EQUITY		Foreign	161.3	58	No load	1.25	2.0	1.4	2.0	56
NORTHERN SMALL CAP GROWTH		Small company	142.3	120	No load	1.00	22.5	20.3	0.6	79
OAKMARK		Growth	3301.6	103	No load	1.22	34.4	33.0	0.9	96
OAKMARK INTERNATIONAL		Foreign	785.8	–27	No load	1.37	8.3	6.0	0.0	47
OBERWEIS EMERGING GROWTH	♦♦	Small company	134.8	50	No load	1.78†	42.6	40.7	0.0	29
OLD WESTBURY INTERNATIONAL		Foreign	102.5	14	4.50	1.50†	2.4	1.9	1.4	59
OPPENHEIMER A	AVG	Growth	259.2	5	5.75	1.29†	24.2	21.1	1.1	207
OPPENHEIMER ASSET ALLOCATION A	♦	Multi-asset global	251.4	6	5.75	1.09†	22.8	20.1	3.6	
OPPENHEIMER DISCOVERY A	♦	Small company	839.6	39	5.75	1.33†	36.8	33.8	0.0	29
OPPENHEIMER EQUITY-INCOME A	AVG	Equity-income	2074.2	21	5.75	0.96†	27.9	25.5	4.3	73
OPPENHEIMER GLOBAL A	♦♦	World	2183.0	18	5.75	1.15†	16.6	14.6	0.6	4
OPPENHEIMER GLOBAL EMERG. GR. A	♦♦♦	World	129.3	–19	5.75	1.77†	5.8	5.8	0.0	4
OPPENHEIMER GLOBAL GRTH. & INC. A	♦	World	108.8	–13	5.75	1.49†	17.4	14.7	2.6	4

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not ran
(jj) Formerly Neuberger & Berman Selected Sectors. (kk) Formerly Nicholas-Applegate Core Growth B. (ll) Formerly Nicholas-Applegate Emerg. Growth B.

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA						RISK	TELEPHONE		
5 YEARS		10 YEARS		BW 10 YEAR	TURNOVER	%CASH	P-E	STYLE	UNTAXED	LARGEST HOLDING		TOLL-FREE	IN-STATE	
AX	PRETAX	AFTERTAX	PRETAX	AFTERTAX	ANALYSIS			RATIO		GAINS (%)	COMPANY (% ASSETS)		(800)		
	14.7	12.2			Very high	11	26	LG	21	Medtronic(6)	Very high	637-3863	NJ	609-282-2800
t rated					Average	16	25	LV	–4	Murata Manufacturing(3)		637-3863	NJ	609-282-2800
					Low	5	29		–50	Grupo Carso (ADR)(3)		637-3863	NJ	609-282-2800
	8.9	8.0			Low	9	28	LB	12	Murata Manufacturing(6)	High	637-3863	NJ	609-282-2800
	19.5	16.6			Average	7	19	SV	4	SLMA(4)	Average	637-3863	NJ	609-282-2800
	20.7	19.1			Average	18	21	SV	8	PXRE(3)	Average	637-3863	NJ	609-282-2800
	11.7	9.0			Average	6	19	LV	18	Mobil(4)	Average	637-3863	NJ	609-282-2800
					Very high	5	37	MG	19	Acclaim Entertainment(11)		637-3863	NJ	609-282-2800
	15.2	12.7			Average	4	18	LV	33	Lockheed Martin(4)	Average	637-2929	MA	617-954-5000
	30.5	29.9			Average	1	29	MG	33	Oracle(6)	High	637-2929	MA	617-954-5000
	14.6	11.5	11.2	7.8	Average	0	23	MB	31	Intel(3)	Average	637-2929	MA	617-954-5000
t rated					High	1	21	MV	26	Promus(5)		637-2929	MA	617-954-5000
	20.0	17.0	14.6	11.1	High	3	25	MG	26	W.R. Grace(2)	Average	637-2929	MA	617-954-5000
	13.7	11.5	12.5	9.8	High	10	19	LV	21	Philip Morris(1)	Very low	637-2929	MA	617-954-5000
	20.8	17.5	15.5	11.9	High	13	20	MV	26	Tyco International(4)	Average	637-2929	MA	617-954-5000
t rated					High	5	21	MV	10	Astra CI B(1)		637-2929	MA	617-954-5000
	9.7	8.5			High	2	21	MB	18	Astra CI B(4)	Average	637-2929	MA	617-954-5000
t rated						10	29	MG	11	Cadence Design Systems(2)		637-2929	MA	617-954-5000
	12.5	10.6			High	10	18	LV	12	PowerGen (ADR)(1)	Low	637-2929	MA	617-954-5000
	14.7	12.6			Very high	24	33	MG	3	Oxford Health Plans(3)	High	666-3882	IL	708-462-9800
t rated					High	0	26	MB	10	General Instrument(3)		572-3863		
					High	3	21	MG	–6	Arab-Malaysian Merchant Bank(2)		572-3863	CA	415-627-2400
t rated					Average	0	27	LG	9	Nokia CI A(5)		572-3863	CA	415-627-2400
t rated					High	24	25	MB	20	Intl. Paper(6)		572-3863		
t rated						34	25	SB	10	Aspect Telecommunications(2)		572-3863	CA	415-627-2400
	26.9	23.9			Average	5	29	SG	31	ALC Communications(7)	High	572-3863	CA	415-627-2400
t rated					Low	0	21	LG	4	Cheung Kong Holdings(5)		282-4404		
	18.8	16.7	15.6	13.2	Average	21	17	MV	18	Chase Manhattan(5)	Very low	553-3014	NJ	201-912-2100
					Average	15	16	SV	18	Getinge(3)		553-3014	NJ	201-912-2100
	19.5	16.9	15.2	11.9	Average	25	17	MV	24	Chase Manhattan(5)	Very low	553-3014	NJ	201-912-2100
	19.1	16.2	15.0	11.6	Average	25	16	LV	30	Chase Manhattan(6)	Very low	553-3014	NJ	201-912-2100
t rated					High	15	20	LV	7	BankAmerica(1)		321-7854		
	13.4	11.2	13.4	10.4	Very low	3	19	LG	35	Warner-Lambert(5)	Average	848-0920	OH	614-249-7855
	16.0	14.3	12.7	10.2	Very low	12	21	LB	33	Intel(8)	Average	848-0920	OH	614-249-7855
t rated						9	30	SG	19	Wireless Telecom Group(4)		887-8671		
	19.3	16.8	14.3	11.1	Low	2	17	LV	37	Citicorp(3)	Average	877-9700	NY	212-476-8800
	18.4	17.1			Average	2	19	SV	30	BMC Industries(5)	Average	877-9700	NY	212-476-8800
	19.5	17.8	14.9	12.1	Low	14	20	LV	28	Citicorp(2)	Average	877-9700	NY	212-476-8800
	16.5	13.4	13.4	10.5	Average	2	22	MB	32	Micron Technology(3)	High	877-9700	NY	212-476-8800
	17.3	14.3	13.8	10.5	High	2	20	MV	27	EXEL(3)	Average	877-9700	NY	212-476-8800
	17.7	15.9	14.0	11.4	Low	14	24	MB	22	Tele-Communications CI A(5)	Average	421-4120	CA	213-486-9200
	15.6	14.0	10.7	8.2	Low	4	16	LV	13	Texas Instruments(2)	Low	225-7670	MA	617-578-1400
					Average	1	28	LG	24	Oracle Systems(3)		225-7670	MA	617-578-1400
	15.9	12.4	13.5	10.3	High	1	16	LV	16	Citicorp(7)	High	225-7670	MA	617-578-1400
	16.0	13.9	12.2	9.0	Very low	3	19	LB	31	Exxon(3)	Low	225-7670	MA	617-578-1400
					High	5	27	LB	2	Acerinox(2)		225-7670	MA	617-578-1400
t rated						11	27	MG	14	Nokia (ADR)(2)		225-7670	MA	617-578-1400
	17.4	15.3	12.3	9.1	Low	4	17	LV	22	Carnival CI A(2)	Average	225-7670	MA	617-578-1400
	15.0	13.5	14.7	12.2	Low	15	23	LG	14	Mannesmann (Germany)(2)	Average	421-4120	CA	213-486-9200
					Very high	–10	35	MG	32	Kemet(6)		222-2872		
	17.4	15.6	13.2	11.1	Low	5	19	MB	39	FNMA(3)	Low		WI	414-272-6133
	16.1	14.2	12.5	10.7	Low	4	22	MB	49	Health Management Assoc CI A(4)	Low		WI	414-272-6133
	18.1	15.8			Very low	2	23	SB	47	Keane(5)	Low		WI	414-272-6133
t rated					High	7	29	MG	19	Safeway(3)		551-8043		
t rated					High	6	31	SG	19	STERIS(1)		551-8043		
					High	6	28	MG	26	Adaptec(2)		225-1852		
t rated						3	23	LB	15	Emerson Electric(3)		595-9111		
t rated						–1	31	LB	–5	Norsk Hydro (ADR)(1)		595-9111		
t rated						0	19	SV	9	FoxMeyer Health()		595-9111		
					Low	7	18	MV	17	Lockheed Martin(6)		625-6275		
					Average	3	13	MV	7	Kvaerner Industrie(5)		625-6275		
	26.3	24.4			Average	0	28	SG	38	ValuJet(5)	Very high	323-6166	IL	708-897-7100
t rated					Low	3	15	MB	–5	Swire Pacific CI A(3)		545-1074		
	14.9	12.6	9.8	6.9	Low	6	20	LB	33	Intel(3)	Average	525-7048	CO	303-671-3200
	11.6	9.7			Low	4	21	LB	19	Intel(2)	Very low	525-7048	CO	303-671-3200
	23.5	22.2			High	12	34	SG	34	Omnicare(2)	High	525-7048	CO	303-671-3200
	12.3	10.2	11.6	8.7	Average	10	14	LV	19	Philip Morris(2)	Low	525-7048	CO	303-671-3200
	12.0	10.2	15.2	12.3	Average	5	20	LB	18	Philips Electronics(2)	High	525-7048	CO	303-671-3200
	5.4	5.3			Average	3	20	SG	–21	Transocean Drilling(2)	Very high	525-7048	CO	303-671-3200
	11.0	9.3			High	5	21	LG	10	Nintendo(2)	Average	525-7048	CO	303-671-3200

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG. 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RAN OB
OPPENHEIMER GOLD & SPEC. MIN. A	▼▼▼	Precious metals	156.7	–12	5.75	1.36	–1.5	–1.6	0.4	
OPPENHEIMER GROWTH A	AVG	Growth	1021.1	50	5.75	1.05†	35.0	31.0	1.2	8
OPPENHEIMER MAIN ST. INC. & GRTH. A	▲▲▲	Growth/income	2465.9	94	5.75	1.07†	30.8	30.0	1.6	8
OPPENHEIMER QUEST GLOBAL VALUE A (mm)	▼	World	161.2	10	5.75	1.95†	20.7	17.8	0.8	
OPPENHEIMER QUEST OPPORT VAL. A (nn)	▲▲▲	Asset allocation	430.8	159	5.75	1.78†	42.0	41.3	0.5	
OPPENHEIMER QUEST SM. CAP VALUE A (oo)	▲	Small company	120.9	1	5.75	1.88†	12.4	10.5	0.6	
OPPENHEIMER QUEST VALUE A (pp)	▲	Growth	295.2	33	5.75	1.71†	37.1	34.4	0.7	5
OPPENHEIMER TARGET A	▼	Maximum growth	757.6	151	5.75	1.16†	34.9	31.1	0.8	
OPPENHEIMER TOTAL RETURN A	AVG	Growth/income	1548.9	25	5.75	1.01†	30.1	27.2	2.3	9
OPPENHEIMER VALUE STOCK A	▲	Growth/income	136.3	47	5.75	1.27†	30.0	28.9	1.7	9
PACIFIC EUROPEAN GROWTH	▼▼	Foreign	160.2	–3	4.00	1.76†	6.0	4.1	0.5	
PACIFIC HORIZON AGGRESSIVE GROWTH	▼▼	Maximum growth	174.3	39	4.50	1.46	43.3	35.5	0.0	
PAINEWEBBER BALANCED A (qq)		Asset allocation	173.0	0	4.50	1.26†	23.3	20.0	2.8	
PAINEWEBBER GLOBAL EQUITY A (rr)		World	332.6	96	4.50	1.58†	13.6	12.5	0.0	
PAINEWEBBER GROWTH & INCOME B (ss)		Growth/income	261.7	4	5.00**	1.97†	32.2	29.7	2.2	6
PAINEWEBBER GROWTH A	▼	Growth	194.8	53	4.50	1.21†	33.5	30.7	0.0	10
PARAGON GULF SOUTH GROWTH A		Growth	93.2	18	4.50	1.00	22.0	21.2	0.0	21
PARAGON VALUE EQUITY-INCOME A	AVG	Growth/income	129.6	29	4.50	0.93	35.2	33.2	2.1	4
PARAGON VALUE GROWTH A	AVG	Growth	200.0	17	4.50	0.96	27.4	24.1	1.1	17
PARKSTONE SMALL CAP INV. A		Small company	101.6	64	4.50	1.55†	35.7	31.1	0.0	
PARNASSUS	AVG	Growth	259.1	61	3.50	1.14	0.6	–0.5	1.7	22
PASADENA GROWTH A	▼▼	Growth	415.6	6	5.50	1.60	27.2	26.6	1.6	18
PASADENA NIFTY FIFTY A	AVG	Growth	122.3	22	5.50	1.90	28.2	28.2	0.0	17
PAX WORLD	AVG	Balanced	477.0	23	No load	0.98†	29.2	27.0	4.8	
PBHG EMERGING GROWTH		Small company	635.6	258	No load‡	1.50	48.4	46.6	0.0	
PBHG GROWTH	▲▲	Small company	2028.1	172	No load	1.50	50.3	50.3	0.0	
PEACHTREE EQUITY		Growth/income	126.8	24	3.75	1.01†	28.1	27.1	1.0	1
PELICAN	▲▲	Growth/income	163.5	53	No load	1.10	29.8	27.7	2.0	9
PENN SQUARE MUTUAL	AVG	Growth/income	297.9	23	4.75	0.99†	29.2	26.3	1.9	10
PENNSYLVANIA MUTUAL	▲▲	Small company	637.2	–17	1.00*	0.98	18.7	14.6	1.3	
PHILADELPHIA	AVG	Growth/income	91.3	13	No load	1.67†	28.3	23.8	2.4	1
PHOENIX BALANCED A	▲	Balanced	2387.0	–1	4.75	0.96†	23.4	20.5	3.0	
PHOENIX CAPITAL APPRECIATION A	AVG	Growth	489.0	19	4.75	1.36†	30.8	26.0	0.3	1
PHOENIX EQUITY OPPORTUNITIES A	AVG	Growth	205.3	21	4.75	1.26†	33.8	30.1	0.0	1
PHOENIX GROWTH A	AVG	Growth	2370.0	17	4.75	1.19†	34.0	31.3	0.9	1
PHOENIX INCOME & GROWTH A	▲	Balanced	503.9	4	4.75	1.16†	23.4	21.6	4.4	
PHOENIX INTERNATIONAL A	▼▼▼	Foreign	131.7	–19	4.75	1.47†	9.8	9.7	0.0	
PHOENIX TOTAL RETURN A	▲▲	Asset allocation	361.6	8	4.75	1.24†	18.2	15.3	3.0	
PHOENIX U.S. STOCK A	▲	Growth	203.5	53	4.75	1.26†	51.7	46.5	0.3	
PHOENIX WORLDWIDE OPPORTUN. A	▼	World	129.1	–1	4.75	1.50†	15.1	13.1	0.0	
PILGRIM MAGNACAP A	AVG	Growth/income	222.9	13	5.75	1.59†	35.2	34.9	0.8	
PIMCO ADVISORS EQUITY-INCOME C	▲▲	Equity-income	183.4	10	1.00**	2.00†	27.6	25.1	1.6	
PIMCO ADVISORS GROWTH C	▼	Growth	1306.0	24	1.00**	1.90†	27.5	23.4	0.0	1
PIMCO ADVISORS INTERNATIONAL C	▼▼▼	Foreign	203.7	–21	1.00**	2.20†	5.8	5.8	0.0	
PIMCO ADVISORS OPPORTUNITY C	AVG	Maximum growth	725.0	32	1.00**‡	1.90†	41.5	33.7	0.0	
PIMCO ADVISORS TARGET C		Growth	819.2	43	1.00**	2.00†	30.3	26.4	0.0	1
PIONEER	▲	Growth/income	2446.2	22	5.75	0.94†	26.6	23.1	1.8	1
PIONEER CAPITAL GROWTH A	▲▲▲	Small company	953.3	118	5.75	1.26†	30.7	27.2	0.4	
PIONEER EQUITY-INCOME A	▲▲▲	Equity-income	280.4	60	5.75	1.24†	32.0	30.7	2.7	
PIONEER GROWTH A	▼▼	Small company	216.7	63	5.75	1.46†	29.8	25.6	0.2	
PIONEER II	▲	Growth/income	5213.8	20	5.75	0.90†	27.2	23.7	1.3	1
PIONEER INCOME A	▲	Balanced	281.7	8	4.50	1.11†	22.0	19.4	6.3	
PIONEER INTERNATIONAL GROWTH A		Foreign	313.6	11	5.75	1.95†	8.1	7.9	0.1	
PIONEER THREE	AVG	Small company	1046.5	8	5.75	0.85	19.3	16.3	1.1	
PIPER EMERGING GROWTH	▼	Small company	250.0	19	4.00	1.24†	39.4	35.7	0.0	
PIPER GROWTH (tt)	▼	Growth	175.2	–1	4.00	1.27†	28.2	21.1	0.4	1
PREFERRED GROWTH		Growth	390.8	62	No load	0.87	28.4	27.2	0.0	1
PREFERRED INTERNATIONAL		Foreign	136.3	27	No load	1.32	9.9	9.5	1.3	
PREFERRED VALUE		Growth/income	229.5	54	No load	0.89	37.5	36.5	1.3	
PREMIER CAPITAL GROWTH (uu)	▼	Growth	540.3	–2	3.00	1.11	11.0	8.3	1.7	2
PREMIER STRATEGIC INVESTING A (vv)	▼▼	Growth	219.7	–4	4.50	1.54	23.7	20.1	1.4	2
T. ROWE PRICE BALANCED	▲▲	Balanced	608.1	55	No load	1.00	24.9	23.1	3.5	
T. ROWE PRICE BLUE CHIP GROWTH		Growth	146.5	276	No load	1.25	37.9	37.3	1.0	
T. ROWE PRICE CAPITAL APPREC.	▲▲▲	Growth/income	864.3	32	No load	1.10	22.6	19.8	3.1	1
T. ROWE PRICE EQUITY INDEX	▲	Growth/income	457.3	69	No load	0.45	37.2	35.6	2.3	
T. ROWE PRICE EQUITY-INCOME	▲▲▲	Equity-income	5214.8	63	No load	0.88	33.4	31.1	3.2	
T. ROWE PRICE EUROPEAN STOCK	▼▼	Europe	531.6	45	No load	1.25	21.9	20.8	1.4	
T. ROWE PRICE GROWTH & INCOME	▲▲	Growth/income	1748.5	42	No load	0.81	30.9	28.6	3.0	
T. ROWE PRICE GROWTH STOCK	▲	Growth	2761.8	34	No load	0.81	31.0	29.1	0.9	1
T. ROWE PRICE INTL. DISCOVERY	▼▼▼	Foreign	302.8	–31	2.00*	1.50	–4.4	–4.6	0.7	

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=No (mm) Formerly Quest for Value Global Equity A. (nn) Formerly Quest for Value Opportunity A. (oo) Formerly Quest for Value Small Cap A. (pp) Formerly Quest for Value A. (qq) Forme ber Asset Allocation A. (rr) Formerly Kidder, Peabody Global Equity A. (ss) Formerly PaineWebber Dividend Growth B. (tt) Formerly Piper Value. (uu) Formerly Dreyfus Capital mier). (vv) Formerly Dreyfus Strategic Investing A.

ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
S RTAX	5 YEARS PRETAX	5 YEARS AFTERTAX	10 YEARS PRETAX	10 YEARS AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE	
.3	6.2	5.9	13.0	11.4		Low	1	35	SG	2	Euro-Nevada Mining(5)	Very high	525-7048	CO	303-671-3200
.8	18.3	16.2	13.0	10.3		Low	24	20	LB	44	Microsoft(3)	Average	525-7048	CO	303-671-3200
.8	30.6	27.6				High	14	24	LB	15	United HealthCare(2)	Average	525-7048		
.8	13.0	11.2				Average	9	21	LB	24	McDonnell Douglas(5)	Average	525-7048	CO	303-671-3200
.3	23.5	22.5				Average	12	16	LV	20	McDonnell Douglas(8)	Low	525-7048	CO	303-671-3200
.2	18.8	17.1				Average	20	20	SV	12	True North Communications(4)	Average	525-7048	CO	303-671-3200
.8	18.2	16.2	13.0	10.9		Average	14	16	LV	29	EXEL(8)	Low	525-7048	CO	303-671-3200
.5	17.0	14.9	11.6	9.3		Low	18	23	MG	26	Microsoft(2)	Average	525-7048	CO	303-671-3200
.2	17.4	15.0	14.6	11.2		High	9	22	LB	20	Philip Morris(2)	Average	525-7048	CO	303-671-3200
.9	15.0	13.4				Very low	10	18	LV	26	Bristol-Myers Squibb(3)	Low	525-7048	CO	303-671-3200
.1	11.3	10.3				Average	3	33	LV	12	Nomura(2)	High	866-7778	MN	612-342-6223
.4	17.9	14.1	16.1	13.8		High	1	26	SB	36	Pyxis(3)	Very high	332-3863		
.5						High	8	17	MV	15	Cooper Tire & Rubber(2)		647-1568	NY	201-902-7341
.9						Average	5	22	LB	10	Roche Holdings(3)		647-1568	NY	201-902-7341
.7						High	12	21	LB	18	Johnson & Johnson(2)		647-1568	NY	201-902-7341
.0	16.9	15.6	13.8	12.1		Low	7	27	MG	26	Viacom Cl B(2)	Average	647-1568	NY	201-902-7341
.0						Average	7	24	SB	31	Medaphis(5)		777-5143		
.1	15.6	13.8				Average	3	15	LV	25	Mobil(4)	Average	777-5143		
.4	15.7	13.9				Average	4	21	LB	30	Intel(5)	Average	777-5143		
not rated						Average	4	37	SG	48	Hollywood Entertainment(5)		451-8377		
.6	22.5	20.3	11.6	9.9		Low	6	20	SV	10	Genus(5)	High	999-3505	CA	415-362-3505
.7	14.6	14.4				Average	2	26	LG	31	Gillette(4)	High	648-8050	CA	818-351-4276
.8	17.5	17.5				Low	3	24	LG	30	Gillette(5)	Average	648-8050	CA	818-351-4276
.0	9.7	7.8	10.6	7.9		Low	12	20	LB	11	Merck(8)	Very low	767-1729	NH	603-431-8022
not rated						Low	17	43	SG	28	Applix(3)		433-0051		
.0	35.1	32.2	22.8	19.1		High	7	46	MG	28	Ascend Communications(3)	Very high	433-0051		
not rated						Low	5	20	LB	18	Texas Instruments(2)		621-8969	PA	404-989-6200
.7	17.5	15.3				Average	2	20	LV	20	Eastman Kodak(3)	Low		MA	617-330-7500
.9	15.1	12.6	12.5	9.3		Low	5	19	LB	27	Motorola(2)	Low	523-8440	PA	610-670-1031
.4	15.0	12.4	11.3	8.1		Low	7	17	SV	41	Alleghany(1)	Low	221-4268	NY	212-355-7311
.8	11.8	10.0	10.2	6.9		Low	18	20	LB	31	Coca-Cola(7)	Low	749-9933	FL	407-395-2155
.1	11.0	9.0	11.8	9.1		High	17	26	LB	12	AT&T(1)	Very low	243-4361	CT	203-253-1000
.2	17.3	15.1				Very high	14	34	MG	22	Aetna Life & Casualty(3)	Average	243-4361	CT	203-253-1000
.5	15.7	12.0	13.0	8.4		High	2	31	MG	22	Cisco Systems(5)	Average	243-4361	CT	203-253-1000
.5	12.9	10.8	13.4	10.8		High	11	24	LB	23	AT&T(2)	Low	243-4361	CT	203-253-1000
.2	12.8	10.4	12.4	9.4		High	7	25	LB	5	Travelers Group(2)	Very low	243-4361	CT	203-253-1000
.9	7.9	6.9				Very high	18	21	MG	7	Winterthur Insurance(2)	High	243-4361	CT	203-253-1000
.7	12.6	10.0				Very high	20	27	LG	10	Merck(2)	Very low	243-4361	CT	203-253-1000
.3	17.8	14.5	13.4	10.1		Very high	2	35	MG	26	3Com(3)	Low	243-4361	CT	203-253-1000
.1	15.3	13.8	6.5	4.3		Very high	8	24	MG	6	UUNET Technologies(3)	Average	243-4361	CT	203-253-1000
.6	15.8	14.4	12.9	10.8		Very low	2	19	LV	47	AFLAC(9)	Average	992-0180		
.3	16.1	14.8				Very high	5	20	LG	18	SmithKline Beecham (Unit)ADR(3)	Low	426-0107	CT	203-352-4900
.9	15.1	12.8	15.0	12.4		High	8	25	LG	27	IBM(4)	Average	426-0107	CT	203-352-4900
.6	7.9	7.1				Average	7	28	LB	–2	TDK(2)	High	426-0107	CT	203-352-4900
.0	31.7	28.8	19.8	17.0		Average	8	28	MG	45	EMC(6)	Very high	426-0107	CT	203-352-4900
.3						High	11	24	MB	27	Hospitality Franchise System(3)		426-0107	CT	203-352-4900
.4	15.0	12.3	11.9	8.6		Low	1	18	MV	39	Ford Motor(3)	Low	225-6292	MA	617-742-7825
.7	25.4	23.1				Average	21	21	SV	17	Toys 'R' Us(2)	Low	225-6292	MA	617-742-7825
.2	17.6	15.9				Low	0	16	LV	13	Bell Atlantic(3)	Very low	225-6292	MA	617-742-7825
.4	17.7	14.6	14.3	11.5		High	21	24	SB	22	Safeguard Scientific(3)	Very high	225-6292	MA	617-742-7825
.6	15.4	12.3	11.6	8.4		Average	4	17	MV	22	IBP(3)	Low	225-6292	MA	617-742-7825
.3	10.4	8.0	9.9	7.0		Average	3	17	LV	7	Allegheny Power System(2)	Very low	225-6292	MA	617-742-7825
not rated						Very high	0	20	LV	1	Korea Mobile Telecom(5)		225-6292	MA	617-742-7825
.9	16.5	14.4	11.6	8.9		Low	8	22	SV	33	Boston Scientific(3)	Average	225-6292	MA	617-742-7825
.2	22.7	22.1				Low	8	30	MG	50	Green Tree Financial(3)	High	866-7778	MN	612-342-6223
.9	14.6	12.9				Average	2	23	LB	40	Enron(4)	Average	866-7778	MN	612-342-6223
.4						Average	1	26	LG	30	Intel(4)		662-4769		
.3						Low	5	14	MV	11	Ciba-Geigy (Br)(2)		662-4769		
.7						Low	7	18	LB	26	Unilever(3)		662-4769		
.9	10.8	7.8	10.4	7.0		Very high	0	19	LV	15	Philip Morris(5)	Low	554-4611	MA	718-895-1396
.2	11.4	9.4				Very high	3	21	MB	17	Amoco(2)	High	554-4611	MA	718-895-1396
.9	12.7	10.4	11.8	8.2		Low	10	21	LB	14	General Electric(1)	Very low	638-5660	MD	410-547-2308
not rated						Average	21	22	LB	18	First Financial Management(2)		638-5660		
.6	14.4	12.1				Average	23	21	MV	18	Automatic Data Processing cv(5)	Very low	638-5660	MD	410-547-2308
.7	16.0	14.9				Very low	15	20	LB	22	General Electric(2)	Average	638-5660	MD	410-547-2308
.6	18.0	15.8	15.1	12.2		Low	16	17	LB	19	SmithKline Beecham (Unit)ADR(2)	Very low	638-5660	MD	410-547-2308
.7	10.3	9.8				Low	4	20	LB	19	Wolters Kluwer(3)	High	638-5660	MD	410-547-2308
.0	17.5	15.7	11.9	9.1		Low	15	20	LB	23	California Federal Bank Cl A(3)	Low	638-5660	MD	410-547-2308
.1	16.7	14.7	13.3	10.4		Average	5	24	LB	38	FHLMC(4)	Average	638-5660	MD	410-547-2308
.1	6.1	5.5				Average	3	23	SB	–6	Ashtead Group(1)	High	638-5660	MD	410-547-2308

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WITH OBJECTIV
T. ROWE PRICE INTL. STOCK		Foreign	6703.3	16	No load	0.96	11.4	10.4	1.4	26/6
T. ROWE PRICE JAPAN		Pacific	207.5	23	No load	1.50	–3.1	–3.1	0.0	20/2
T. ROWE PRICE LATIN AMERICA		Foreign	149.5	–9	2.00*	1.82	–18.7	–18.9	0.9	63/6
T. ROWE PRICE MID-CAP GROWTH		Growth	264.0	163	No load	1.25	41.0	39.5	0.0	20/22
T. ROWE PRICE NEW AMERICA GROWTH	AVG	Growth	1028.2	59	No load	1.14	44.3	42.4	0.0	11/22
T. ROWE PRICE NEW ASIA		Pacific	1880.3	–5	No load	1.15	3.8	3.4	1.1	11/2
T. ROWE PRICE NEW ERA		Natural resources	1090.4	11	No load	0.80	20.8	18.4	2.0	8/1
T. ROWE PRICE NEW HORIZONS		Small company	2854.5	73	No load	0.93	55.4	50.9	0.0	6/9
T. ROWE PRICE OTC SECURITIES		Small company	278.6	42	No load	1.11	33.8	29.5	0.7	38/9
T. ROWE PRICE SCIENCE & TECH.		Technology	2285.3	150	No load	1.11	55.5	49.7	0.0	3/1
T. ROWE PRICE SMALL-CAP VALUE		Small company	936.4	129	No load	0.97	29.3	27.6	1.1	54/9
T. ROWE PRICE SPECTRUM GROWTH		Growth	1358.3	54	No load	0.00	30.0	27.5	1.5	147/22
T. ROWE PRICE SPECTRUM INCOME		Asset allocation	986.7	58	No load	0.00	19.4	17.0	6.3	29/3
PRINCOR CAPITAL ACCUMULATION A		Growth	364.1	30	4.75	0.83†	31.9	29.1	1.7	126/22
PRINCOR EMERGING GROWTH A		Maximum growth	162.7	72	4.75	1.74†	34.2	33.2	0.4	23/3
PRINCOR GROWTH A		Growth	188.8	61	4.75	1.30†	33.5	32.0	0.9	108/22
PRINCOR WORLD A		Foreign	132.1	19	4.75	1.74†	11.6	9.8	1.0	22/6
PRUDENTIAL ALLOCATION BAL. B (ww)	AVG	Asset allocation	441.8	3	5.00**	1.97†	16.7	14.7	2.0	31/3
PRUDENTIAL ALLOCATION STRATEGY B	AVG	Asset allocation	268.9	–16	5.00**	2.08†	21.3	18.6	1.6	25/3
PRUDENTIAL EQUITY B		Growth	2148.4	9	5.00**	1.75†	30.6	28.8	0.9	140/22
PRUDENTIAL EQUITY-INCOME B		Equity-income	935.9	2	5.00**	1.85†	20.7	18.3	2.4	33/3
PRUDENTIAL EUROPE GROWTH B		Europe	123.1	18	5.00**	1.59†	16.5	16.5	0.0	7/1
PRUDENTIAL GLOBAL B		World	263.2	–30	5.00**	2.24†	14.2	12.6	0.0	24/4
PRUDENTIAL GLOBAL GENESIS B		World	148.5	–17	5.00**	2.17†	9.8	9.7	0.5	34/4
PRUDENTIAL GROWTH OPPORTUNITY B	AVG	Small company	346.2	–11	5.00**	2.08†	23.3	21.6	0.0	74/9
PRUDENTIAL MULTI-SECTOR B	AVG	Growth	240.0	40	5.00**	2.19†	19.8	15.9	0.2	225/22
PRUDENTIAL PACIFIC GROWTH B		Pacific	348.8	–15	5.00**	2.33†	4.7	4.3	0.0	8/2
PRUDENTIAL UTILITY B	AVG	Utilities	2356.6	–33	5.00**	1.63†	24.8	23.3	2.2	20/2
PUTNAM ASIA PACIFIC GROWTH A		Pacific	163.1	5	5.75	1.53†	2.8	1.4	4.5	15/2
PUTNAM ASSET ALLOC.: BALANCED A		Multi-asset global	191.8	151	5.75	NA†	24.1	22.0	2.9	4/1
PUTNAM ASSET ALLOC.: GROWTH A		Multi-asset global	141.9	147	5.75	NA†	25.8	24.2	1.8	2/1
PUTNAM BALANCED RETIREMENT A (xx)		Balanced	482.2	11	5.75	1.08†	27.0	24.7	4.4	20/5
PUTNAM CAPITAL APPRECIATION A		Growth	125.3	237	5.75	1.13†	34.5	33.4	0.9	93/22
PUTNAM DIVERSIFIED EQUITY B		Growth	135.9	116	5.00**	1.45†	28.1	26.7	0.5	171/22
PUTNAM EQUITY INCOME A		Equity-income	402.7	31	5.75	1.04†	34.6	33.5	2.9	3/3
PUTNAM EUROPE GROWTH A		Europe	99.6	19	5.75	1.38†	21.2	20.3	0.0	4/1
PUTNAM FUND FOR GROWTH & INC. A		Growth/income	8610.6	47	5.75	0.95†	36.5	33.9	2.4	24/13
PUTNAM GLOBAL GROWTH A		World	1785.5	21	5.75	1.33†	14.8	13.0	1.7	22/4
PUTNAM GROWTH & INCOME II B		Growth/income	296.0	NM	5.00**	NA†	33.0	31.4	1.2	60/13
PUTNAM HEALTH SCIENCES A		Health care	1140.6	44	5.75	1.12†	47.0	45.9	0.6	5/
PUTNAM INVESTORS A	AVG	Growth	1022.2	33	5.75	0.99†	37.5	32.8	0.9	51/22
PUTNAM NATURAL RESOURCES A		Natural resources	152.3	29	5.75	1.13†	24.7	23.8	2.0	5/1
PUTNAM NEW OPPORTUNITIES A		Growth	2363.0	157	5.75	1.13†	46.2	46.2	0.0	7/22
PUTNAM OTC EMERGING GROWTH A	AVG	Small company	997.9	95	5.75	1.14†	55.9	51.5	0.0	5/9
PUTNAM PREFERRED INCOME A (yy)		Equity-income	115.1	0	3.25	0.81	16.6	14.9	6.2	34/3
PUTNAM UTILITIES GROWTH & INC. A	AVG	Utilities	629.4	21	5.75	1.08†	31.1	29.4	4.2	8/2
PUTNAM VISTA A		Growth	996.3	46	5.75	1.07†	39.4	36.0	0.0	29/22
PUTNAM VOYAGER A		Maximum growth	5986.2	73	5.75	1.07†	40.2	38.1	0.0	9/3
REICH & TANG EQUITY		Growth	109.5	18	No load	1.17†	28.2	24.5	1.1	168/22
RIGHTIME		Growth/income	155.4	9	No load	2.51†	26.9	25.3	1.9	120/13
RIGHTIME BLUE CHIP		Growth/income	254.1	15	4.75	2.22†	29.0	27.7	0.8	107/13
ROBERTSON STEPHENS CONTRARIAN		Multi-asset global	508.4	5	0.50*	2.46†	30.9	30.9	0.0	1/1
ROBERTSON STEPHENS EMERGING GRTH.		Small company	158.5	–10	0.50*	1.56†	20.3	17.7	0.0	82/9
ROBERTSON STEPHENS VALUE + GRTH.		Growth	1144.4	764	0.50*	1.68	42.7	42.7	0.0	14/22
ROYCE MICRO-CAP		Small company	97.5	264	1.00*	1.99	19.1	18.3	0.0	88/9
ROYCE PREMIER		Small company	302.1	49	1.00*	1.38	17.8	15.6	1.2	94/9
ROYCE VALUE		Small company	166.8	0	1.00*	1.80†	18.7	16.3	0.5	89/9
RYDEX NOVA		Maximum growth	222.5	281	No load	1.43	50.4	47.9	1.6	3/
RYDEX URSA		Asset allocation	117.9	–17	No load	1.39	–20.1	–20.7	2.5	34/
SAFECO EQUITY		Growth/income	619.8	38	No load	0.84	25.3	21.5	2.1	127/1
SAFECO GROWTH		Small company	183.0	22	No load	0.98	26.1	16.8	0.3	68/9
SAFECO INCOME		Equity-income	229.6	27	No load	0.87	30.4	27.2	4.0	15/
SALOMON BROS. CAPITAL		Growth	97.3	–1	No load	1.30	34.8	30.6	0.7	87/2
SALOMON BROS. INVESTORS O	AVG	Growth/income	385.5	5	No load‡	0.69	35.0	31.4	1.2	45/1
SALOMON BROS. OPPORTUNITY		Growth	133.2	16	No load	1.22	35.1	33.3	1.3	82/2
SBSF		Growth/income	116.9	8	No load	1.23†	32.6	28.1	0.7	64/1
SCHWAB 1000		Growth/income	1063.4	92	0.50*	0.54	36.6	36.0	1.4	21/1
SCHWAB INTERNATIONAL INDEX		Foreign	195.9	42	0.75*	0.85	14.2	13.8	1.1	12/
SCHWAB SMALL CAP INDEX		Small company	138.5	96	0.50*	0.68	27.7	27.5	0.5	61/
SCOUT STOCK (zz)		Growth/income	146.4	21	No load	0.86	19.7	16.5	2.9	135/1

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not mea (ww) Formerly Prudential Allocation Conserv. Mgd. B.(xx) Formerly Putnam Managed Income A.(yy) Formerly Putnam Corporate Asset.(zz) Formerly UMB Stock.

E ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
S ERTAX	5 YEARS PRETAX	5 YEARS AFTERTAX	10 YEARS PRETAX	10 YEARS AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE	
.4	11.6	10.2	14.9	11.6		Low	6	26	LB	11	Wolters Kluwer(2)	High	638-5660	MD	410-547-2308
.8						Average	7	42	LB	–7	Kyocera(4)		638-5660	MD	410-547-2308
not rated						Low	7	20		–49	Telefonos de Mexico L (ADR)(8)		638-5660		
.4						Average	12	28	MG	25	First Financial Management(3)		638-5660	MD	410-547-2308
.0	22.8	21.8	15.3	14.2		Low	3	28	MG	39	CUC International(4)	High	638-5660	MD	410-547-2308
.0	14.8	13.5				Average	4	19	MB	–5	Hutchison Whampoa(4)	Very high	638-5660	MD	410-547-2308
.5	11.4	9.3	11.4	8.7		Low	8	24	LB	29	Wal-Mart Stores(5)	Average	638-5660	MD	410-547-2308
.0	26.2	22.9	14.5	11.4		Average	8	33	MG	40	Paychex(3)	High	638-5660	MD	410-547-2308
.2	20.2	16.1	10.7	7.3		Average	13	22	SB	35	Selective Insurance Group(2)	Average	638-5660	MD	410-547-2308
.5	33.6	30.9				High	6	38	MG	37	First Financial Management(5)	High	638-5660	MD	410-547-2308
.6	20.6	19.1				Low	23	19	SV	22	Electro Rent(2)	Very low	638-5660	MD	410-547-2308
.5	17.3	15.1				Low	0	25	LB	17	T. Rowe Price Growth Stock(23)	Low	638-5660	MD	410-547-2308
.2	11.2	8.6				Low	12	18	LV	3	T. Rowe Price New Income(28)	Very low	638-5660	MD	410-547-2308
.3	16.3	14.2	11.7	9.1		Low	2	20	LB	21	General Electric(3)	Low	451-5447	IA	515-247-6833
.4	22.2	21.6				Very low	12	24	SB	30	Boston Scientific(4)	Average	451-5447	IA	515-247-6833
.5	20.6	19.2	14.6	12.6		Very low	5	26	LG	34	Boston Scientific(4)	Average	451-5447	IA	515-247-6833
.6	12.4	11.4	11.2	8.3		Very low	5	13	MV	16	Unilever(2)	High	451-5447	IA	515-247-6833
.8	10.7	8.6				Very high	32	23	MB	13	SunAmerica(2)	Low	225-1852		
.1	10.8	8.7				Very high	2	23	MB	19	SunAmerica(2)	Low	225-1852		
.4	17.5	15.6	14.1	11.8		Very low	12	18	LV	31	Scott Paper(4)	Average	225-1852		
.9	14.5	12.4				Average	8	22	MV	8	McDermott International(3)	Low	225-1852		
not rated						Very low	11	19	MG	14	Sidel(5)		225-1852		
.2	11.2	10.8	10.4	9.4		Average	8	24	LG	37	Samsung Electronics(2)	High	225-1852		
.6	13.0	12.9				Average	19	22	SG	15	Sidel(3)	High	225-1852		
.2	18.6	16.4	11.9	10.0		Average	11	19	SV	17	Precision Castparts(5)	Average	225-1852		
.2	14.0	11.3				High	6	22	MB	12	SunAmerica(3)	Average	225-1852		
.7						Average	5	25	LB	8	Western Mining(5)		225-1852		
.8	11.3	9.6	12.6	10.1		Very low	2	17	MV	22	Sonat(3)	Low	225-1852		
.9						Average	4	29	LB	1	United Overseas Bank(2)		225-1581		
not rated							2	21	LB	10	Philip Morris(1)		225-1581	MA	617-292-1000
not rated							2	21	MB	11	Philip Morris(1)		225-1581	MA	617-292-1000
.1	14.3	11.7	10.6	6.9		High	2	18	LV	9	Exxon(1)	Very low	225-1581	MA	617-292-1000
not rated						Very low	4	19	MB	16	General Electric(2)		225-1581	MA	617-292-1000
not rated						Average	4	24	MB	15	Bear Stearns(1)		225-1581	MA	617-292-1000
.7	15.9	14.4	11.0	7.5		Average	3	18	LV	–16	J. P. Morgan(2)	Low	225-1581	MA	617-292-1000
.6	13.8	13.0				Average	0	16	MV	21	Repsol(3)	Average	225-1581	MA	617-292-1000
.6	15.7	13.3	14.6	10.8		Average	6	18	LB	18	Philip Morris(3)	Low	225-1581	MA	617-292-1000
.3	12.2	11.2	12.4	10.5		Low	6	24	LB	13	Veba(1)	Average	225-1581	MA	617-292-1000
not rated							3	18	LB		Eastman Kodak(3)		225-1581	MA	617-242-1000
.4	17.6	16.2	17.4	15.1		Low	4	27	LG	42	Johnson & Johnson(6)	High	225-1581	MA	617-292-1000
.1	16.7	12.8	13.8	9.0		High	4	22	LB	28	IBM(2)	Average	225-1581	MA	617-292-1000
.6	9.5	7.3	9.9	8.0		Average	2	21	LV	5	Exxon(6)	High	225-1581	MA	617-292-1000
.8	33.4	32.9				Average	7	37	MG	29	America Online(2)	High	225-1581	MA	617-292-1000
.9	27.3	24.5	18.8	16.6		High	5	42	MG	41	US Robotics(5)	High	225-1581	MA	617-292-1000
.8	10.9	8.5	7.8	4.7		Low	6	22	MB	–54	Kmart(1)	Very low	225-1581	MA	617-292-1000
.7	11.3	9.3				High	3	20	LV	8	Sprint(5)	Low	225-1581	MA	617-292-1000
.5	20.6	17.7	15.7	12.4		High	6	28	MG	28	DSC Communications(2)	Average	225-1581	MA	617-292-1000
.1	22.4	20.9	18.3	15.7		Average	2	31	MG	32	Tele-Communications Cl A(2)	Average	225-1581	MA	617-292-1000
.5	16.4	13.5	13.4	10.2		Low	8	22	MB	29	Corning(4)	Low	676-6779	NY	212-830-5220
.9	13.4	10.7	10.8	8.5		Very low	0	25	LG	17	Fidelity Magellan(7)	Low	242-1421	PA	215-887-8111
.8	12.6	11.0				Very low	0	20	LB	15	General Electric(2)	Very low	242-1421	PA	215-887-8111
not rated						Average	26	26	SB	7	Diamond Fields Res (Canada)(25)		766-3863	CA	415-781-9700
.7	16.6	14.9				Very high	16	34	SG	22	PacifiCare Health Sys Cl B(3)	Very high	766-3863	CA	415-781-9700
.3						Very high	1	28	MG	24	Applied Materials(6)		766-3863	CA	415-781-9700
.4						Average	15	16	SV	9	Conso Products(2)		221-4268	NY	212-355-7311
.9						Average	17	17	SV	12	Comdisco(2)		221-4268	NY	212-355-7311
.9	14.4	12.5	10.0	7.6		Low	5	18	SV	33	Alleghany(1)	Low	221-4268	NY	212-355-7311
not rated						Very low	0	NA		19	S & P 500 Futures 450(8)		820-0888	MD	301-652-4402
not rated						Very low	0	NA		–11	S&P 500 Sept 575 (Put)()		820-0888	MD	301-652-4402
.0	20.3	17.8	15.4	12.2		Average	4	18	LV	18	Philip Morris(5)	Average	426-6730	WA	206-545-5530
.5	19.0	15.6	12.4	9.0		High	3	19	SV	13	Canandaigua Wine Cl A(10)	Very high	426-6730	WA	206-545-5530
.1	14.8	12.8	11.0	8.6		Low	3	18	LV	20	GTE(4)	Low	426-6730	WA	206-545-5530
.1	13.6	11.1	10.2	7.2		High	10	19	LV	19	Stop & Shop(3)	High	725-6666	NY	212-783-2081
.5	16.5	12.6	12.6	8.5		Average	6	19	LV	29	Stop & Shop(4)	Average	725-6666	NY	212-783-1301
.4	18.0	16.3	12.3	9.9		Very low	10	15	LV	55	Chubb(11)	Low	725-6666	NY	212-783-1301
.2	13.9	10.4	11.8	8.8		Average	5	24	MV	26	American International Group(8)	Low	422-7273	NY	212-903-1200
.7						Very low	1	21	LB	24	General Electric(2)		526-8600		
not rated						Very low	1	30	LB	11	Royal Dutch Petroleum (Br)(2)		526-8600		
not rated						Low	1	23	SB	15	Hillhaven§		526-8600		
.1	12.7	10.5	11.1	8.4		Average	26	21	MV	13	AT&T(1)	Low	422-2766	MO	816-471-5200

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK WITH OBJECTIVE
SCUDDER CAPITAL GROWTH		Growth	1565.1	21	No load	0.97	31.6	26.2	0.3	130/229
SCUDDER DEVELOPMENT		Small company	877.2	46	No load	1.32	50.7	46.6	0.0	7/99
SCUDDER GLOBAL	AVG	World	1271.9	14	No load	1.38	20.5	19.2	0.9	10/41
SCUDDER GLOBAL SMALL COMPANY		World	253.1	8	No load	1.70	17.8	16.6	1.1	14/41
SCUDDER GOLD		Precious metals	117.0	–10	No load	1.65	13.2	8.7	8.9	2/15
SCUDDER GROWTH & INCOME		Growth/income	3068.0	54	No load	0.86	31.2	29.3	2.7	80/138
SCUDDER INTERNATIONAL		Foreign	2352.0	4	No load	1.19	12.2	11.1	0.9	18/66
SCUDDER LATIN AMERICA		Foreign	514.9	–21	2.00*	2.01	–9.8	–10.1	0.9	61/66
SCUDDER PACIFIC OPPORTUNITIES		Pacific	378.0	–10	No load	1.81	1.3	1.1	0.6	17/22
SCUDDER QUALITY GROWTH		Growth	185.8	65	No load	1.25	32.5	31.0	0.7	120/229
SEAFIRST RETIREMENT ASSET ALLOC.		Asset allocation	147.1	2	No load	0.78	26.5	23.0	3.1	12/34
SEAFIRST RETIREMENT BLUE CHIP	AVG	Growth	181.5	27	No load	0.82	35.7	32.3	1.4	71/229
SECURITY EQUITY A	AVG	Growth	478.5	37	5.75	1.06	38.4	35.4	0.9	37/229
SELECTED AMERICAN		Growth/income	925.0	75	No load	1.26†	38.1	37.2	1.2	5/138
SELIGMAN CAPITAL A		Maximum growth	215.7	33	4.75	1.13†	37.3	32.4	0.0	12/34
SELIGMAN COMMON STOCK A	AVG	Growth/income	614.4	20	4.75	0.85†	28.2	25.0	2.4	112/138
SELIGMAN COMMUNICATIONS & INFO. A		Technology	1940.7	531	4.75‡	1.65†	43.4	40.2	0.0	11/14
SELIGMAN FRONTIER A	AVG	Small company	335.3	421	4.75	1.43†	36.4	35.1	0.0	29/99
SELIGMAN GROWTH A		Growth	597.5	16	4.75	0.90†	28.5	24.7	0.2	160/229
SELIGMAN HENDERSON GLOB. SM. CO. A		World	118.6	145	4.75	1.92†	25.8	23.4	0.0	2/41
SELIGMAN HENDERSON GLOB. TECH. A		Technology	472.1	655	4.75	2.00†	45.1	42.4	0.2	9/14
SELIGMAN INCOME A		Asset allocation	318.3	11	4.75	1.02†	20.6	18.1	5.2	27/34
SENTINEL BALANCED		Balanced	272.2	19	5.00	1.21†	25.2	23.1	3.4	30/57
SENTINEL COMMON STOCK	AVG	Growth/income	1069.7	27	5.00	1.02†	34.4	30.7	2.0	48/138
SEQUOIA		Growth	2185.5	41	No load‡	1.00	41.4	41.2	0.4	16/229
SEVEN SEAS MATRIX EQUITY		Growth	211.5	53	No load	0.68†	28.2	23.9	1.7	167/229
SEVEN SEAS S&P 500 INDEX		Growth/income	532.3	76	No load	0.19†	36.4	35.0	1.8	27/138
1784 GROWTH & INCOME		Growth/income	271.4	41	No load	0.94†	30.0	29.6	0.9	98/138
SIERRA EMERGING GROWTH A		Small company	233.0	59	4.50	1.68†	32.2	30.7	0.0	44/99
SIERRA GROWTH & INCOME A		Growth/income	176.3	16	4.50	1.56†	31.1	28.2	0.8	81/138
SIERRA GROWTH A		Growth	162.3	33	4.50	1.76†	36.2	31.7	0.0	63/229
SIFE TRUST		Financial	614.2	50	5.00	0.94	49.5	43.5	2.7	2/7
SIT GROWTH		Growth	377.1	24	No load	0.83	33.6	30.1	0.0	107/229
SKYLINE SPECIAL EQUITIES		Small company	175.5	–13	No load‡	1.49	13.8	12.0	0.0	97/99
SMALLCAP WORLD	AVG	World	4765.7	37	5.75	1.13†	22.7	19.2	0.9	3/41
SMITH BARNEY AGGRESSIVE GROWTH A		Maximum growth	294.3	69	5.00	1.37†	35.8	32.5	0.0	18/34
SMITH BARNEY APPRECIATION A	AVG	Growth	1902.2	21	5.00	1.02†	29.2	25.8	1.5	152/229
SMITH BARNEY EQUITY INCOME A (aaa)		Growth/income	614.0	12	5.00	0.96†	33.1	29.3	2.6	57/138
SMITH BARNEY FUNDAMENTAL VALUE B		Growth	568.3	54	5.00**	2.06†	27.1	25.1	1.5	183/229
SMITH BARNEY GROWTH & INCOME B		Growth/income	110.0	22	5.00**	1.90†	30.3	29.2	1.1	89/138
SMITH BARNEY INTL. EQUITY A		Foreign	489.0	6	5.00	1.35†	2.6	2.3	1.1	56/66
SMITH BARNEY PREMIUM TOTAL RET. B		Equity-income	1858.1	33	5.00**	1.66†	21.9	19.3	7.0	32/34
SMITH BARNEY PRINCIPAL RET 1998		Balanced	93.5	3	5.00‡	1.01	20.2	16.6	5.1	54/57
SMITH BARNEY SPECIAL EQUITIES B		Small company	170.5	81	5.00**	2.21†	62.2	61.1	0.0	2/99
SMITH BARNEY STRAT. INVESTORS B		Asset allocation	223.6	5	5.00**	2.00†	24.0	22.3	2.2	18/34
SMITH BARNEY TELECOMM. GROWTH B		Communications	155.4	–16	5.00**	2.07†	7.7	7.2	0.0	7/7
SMITH BARNEY UTILITIES B	AVG	Utilities	1675.7	12	5.00**	1.56†	30.1	28.2	4.3	12/26
SOGEN INTERNATIONAL		Multi-asset global	2613.3	43	3.75	1.26†	15.2	13.2	3.2	15/18
SOGEN OVERSEAS		Foreign	542.7	24	3.75	1.40†	11.8	10.2	3.5	21/66
SOUTHTRUST VULCAN STOCK		Growth	172.0	44	5.50*	0.48	36.5	34.7	1.6	57/229
STAGECOACH ASSET ALLOCATION A		Asset allocation	1078.0	20	4.50	0.84†	29.2	27.7	3.5	6/34
STAGECOACH CORPORATE STOCK	AVG	Growth/income	327.2	38	No load	0.97†	36.0	34.8	1.4	30/138
STAGECOACH GROWTH & INCOME A	AVG	Growth/income	176.5	55	4.50	1.11†	28.9	27.1	1.1	109/138
STAGECOACH LIFEPATH 2020 RET.		Asset allocation	109.0	89	No load	1.20†	27.1	25.6	2.3	11/34
STAGECOACH LIFEPATH 2040 RET.		Asset allocation	119.5	154	No load	1.20†	32.2	30.7	1.2	4/34
STAR RELATIVE VALUE		Growth/income	136.6	75	4.50	1.15†	35.7	34.9	1.8	34/138
STATE ST. RESEARCH CAPITAL APPR. A (bbb)		Maximum growth	332.8	30	4.50	1.55†	31.2	27.3	0.0	25/34
STATE ST. RESEARCH CAPITAL B		Maximum growth	231.5	187	5.00**	2.08†	30.9	27.9	0.0	26/34
STATE ST. RESEARCH INVESTMENT B (ccc)		Growth/income	165.5	55	5.00**	1.64†	31.9	28.0	0.6	68/138
STATE ST. RESEARCH MGD. ASSETS A (ddd)		Asset allocation	198.1	11	4.50	1.25†	22.8	21.2	2.6	22/34
STEINROE CAPITAL OPPORTUNITIES		Maximum growth	332.5	93	No load	1.05	50.8	49.0	0.0	1/34
STEINROE GROWTH STOCK (eee)	AVG	Growth	375.1	24	No load	0.99	35.6	32.3	0.4	74/229
STEINROE INTERNATIONAL		Foreign	91.2	23	No load	1.59	3.9	3.5	1.2	53/66
STEINROE PRIME EQUITIES		Growth/income	151.7	25	No load	0.96	30.2	26.6	1.6	91/138
STEINROE SPECIAL	AVG	Growth	1133.9	–3	No load	1.02	18.7	16.1	0.4	226/229
STEINROE TOTAL RETURN		Equity-income	227.5	6	No load	0.87	22.7	20.3	4.1	31/34
STI CLASSIC CAPITAL GROWTH INV.		Growth	175.4	16	3.75	1.80†	30.3	28.6	0.4	143/229
STI CLASSIC VALUE INC. STOCK INV.		Equity-income	112.8	53	3.75	1.30†	35.5	31.2	2.3	2/34
STOCK & BOND		Balanced	136.9	12	No load	1.06	25.1	21.4	3.3	31/57
STRATTON MONTHLY DIVIDEND	AVG	Equity-income	128.7	6	No load	1.08	23.4	20.9	7.1	30/34

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not meaningful. (aaa) Formerly Smith Barney Income & Growth A. (bbb) Formerly MetLife-State St. Research Cap Appr. A. (ccc) Formerly State Street Investment B. (ddd) Formerly MetLife-State St. Research Mgd. Assets A. (eee) Formerly SteinRoe Stock.

ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
	5 YEARS		10 YEARS										TOLL-FREE	IN-STATE	
TAX	PRETAX	AFTERTAX	PRETAX	AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		(800)		
4	16.9	14.1	13.8	10.7		Average	2	19	LB	26	FNMA(3)	High	225-2470	MA	617-439-4640
1	21.2	19.0	14.5	12.4		Average	2	34	SG	43	Informix(3)	Very high	225-2470	MA	617-439-4640
0	13.1	12.1				Average	8	26	LB	21	BBC Brown Boveri (Br)(2)	Average	225-2470	MA	617-439-4640
9						Average	11	27	SG	20	Atmel(4)		225-2470	MA	617-439-4640
2	7.2	5.8				Average	2	39	SG	4	Stillwater Mining (144A)(6)	Very high	225-2470	MA	617-439-4640
5	16.9	14.8	14.0	10.6		Average	–1	19	LB	20	United Technologies(2)	Low	225-2470	MA	617-439-4640
9	10.1	9.0	12.9	10.2		Average	4	26	LB	20	Canon(1)	High	225-2470	MA	617-439-4640
0						Low	15	26		–22	Perez Cl B(5)		225-2470	MA	617-439-4640
2						Average	4	23	MG	1	PTT Exploration/Production(3)		225-2470	MA	617-439-4640
9						High	4	22	LB	19	American International Group(3)		225-2470	MA	617-439-4640
5	11.6	9.8				High	6	20	LB	13	Motorola(2)	Very low	323-9919	NY	206-358-6234
1	15.2	13.6				Average	3	20	LB	22	General Electric(3)	Low	323-9919	NY	206-358-6234
8	18.2	14.9	15.0	11.0		Average	4	21	LB	29	Cabot(2)	Average	888-2461	KS	913-295-3127
9	16.9	14.0	13.7	10.5		Low	1	18	LV	24	Intel(4)	Average	243-1575	NM	505-983-4335
7	18.2	14.5	13.8	10.6		Average	1	25	MG	39	Intel(4)	High	221-2783	NY	212-850-1864
3	14.7	12.2	12.5	8.9		Average	4	20	LB	31	General Electric(2)	Average	221-2783	NY	212-850-1864
4	36.6	32.1	23.0	18.9		High	3	23	MG	27	EMC(4)	Very high	221-2783	NY	212-850-1864
9	26.2	22.3	16.6	14.2		Average	9	28	SG	12	Cognex(2)	High	221-2783	NY	212-850-1864
5	15.1	11.7	12.7	8.8		High	2	24	LG	33	Intel(3)	Average	221-2783	NY	212-850-1864
6						Average	8	26	SG	18	Altera(3)		221-2450	NY	212-850-1864
ot rated							15	27	MG	23	Altera(2)		221-2450	NY	212-850-1864
5	15.1	12.7	10.3	7.2		Average	7	16	LV	8	FPL Group(1)	Very low	221-2783	NY	212-850-1864
2	11.6	9.9	10.7	8.5		Average	8	19	LV	18	Sears Roebuck(2)	Very low	282-3863	VT	802-229-3900
9	15.0	12.8	13.3	10.7		Very low	5	19	LB	50	Kimberly-Clark(3)	Average	282-3863	VT	802-229-3900
3	20.4	18.4	15.4	12.7		Low	3	19	MV	47	Berkshire Hathaway(31)	Low		NY	212-832-5280
1						High	5	18	LB	11	Exxon(4)		647-7327	MA	617-654-6089
7						Average	0	20	LB	16	General Electric(2)		647-7327	MA	617-654-6089
ot rated						Average	7	26	LG	21	Home Depot(3)		252-1784		
6	21.0	19.8				Very high	2	28	SG	22	RP Scherer(6)	Average	222-5852		
4	13.9	11.8				Average	3	20	LB	14	ITT(2)	Average	222-5852		
ot rated						Very high	9	26	MG	25	Astra Cl A Free(4)		222-5852		
4	25.5	22.7	14.3	11.7		Low	6	14	MV	43	Integra Financial(3)	Average	524-7433	CA	510-937-3964
9	18.5	17.1	14.7	12.8		Average	4	34	MG	42	3Com(4)	High	332-5580	MN	612-334-5888
1	23.7	20.1				Average	5	16	SV	11	PennCorp Financial Group(2)	Average	458-5222	IL	312-913-0900
5	17.1	15.3				Average	18	24	SG	23	Wisconsin Central Transport(1)	Average	421-4120	CA	213-486-9200
1	18.6	17.6	16.6	14.7		Average	3	29	MG	43	Chiron(7)	Very high	451-2010	NY	212-723-9218
3	13.3	11.7	13.4	11.6		Average	14	20	LB	34	Eastman Kodak(4)	Low	451-2010	NY	212-723-9218
5	15.0	12.6	12.0	9.2		Low	7	19	LV	25	Sears Roebuck(4)	Low	451-2010	NY	212-723-9218
6						High	24	17	LV	11	American Express(3)		451-2010	NY	212-723-9218
4						High	4	20	LB	21	Hewlett-Packard(3)		451-2010	NY	212-723-9218
3	14.6	13.6				Low	2	25	MG	5	Nokia Cl A(2)	High	451-2010	NY	212-723-9218
2	15.1	12.5	12.1	9.0		Average	12	17	LV	15	Loews(4)	Very low	451-2010	NY	212-723-9218
5						Very low	–8	20	LB	15	Eastman Kodak(2)		451-2010	NY	212-723-9218
6	25.9	25.6	11.8	10.8		High	8	45	MG	43	Baby Superstore(7)	Very high	451-2010	NY	212-723-9218
5	13.4	10.8				High	12	18	LV	13	IBM(2)	Low	451-2010	NY	212-723-9218
0						Low	3	31	MG	8	LM Ericsson Telephone (ADR)(4)		451-2010	NY	212-723-9218
2	11.2	9.1				Low	2	14	LV	10	Southern(4)	Low	451-2010	NY	212-723-9218
9	13.8	12.2	13.6	10.8		Very low	12	24	SB	16	Bank for Intl. Settlements(1)	Very low	628-0252	NY	212-278-5800
ot rated						Very low	3	23	MV	7	Bank for Intl. Settlements (Reg)(2)		628-0252	NY	212-278-5800
4						Average	10	22	LG	14	Mobil(4)		239-7470		
6	13.5	11.7				Average	29	20	LB	12	General Electric(1)	Very low	222-8222		
9	15.2	14.3	13.4	12.9		Very low	1	20	LB	41	General Electric(2)	Average	222-8222		
5	14.6	13.5				Average	7	20	LB	18	Household International(3)	Average	222-8222		
ot rated							7	22	LB	12	Daimler-Benz (ADR)(1)		222-8222		
ot rated							1	20	LB	14	General Electric(2)		222-8222		
8						Low	0	17	LV	20	Procter & Gamble(4)		677-3863	PA	513-867-5134
4	24.5	22.2				Very high	4	30	MG	30	Texas Instruments(6)	Very high	882-0052	MA	617-357-7800
ot rated						Very high	10	29	MG	9	Texas Instruments(6)		882-0052	MA	617-357-7800
ot rated						Low	5	22	LB	40	Philip Morris(3)		882-0052	MA	617-357-7800
2	13.0	11.1				High	5	25	MB	12	Perkin-Elmer(1)	Low	882-0052	MA	617-357-7800
9	26.2	25.9	14.3	12.4		Average	11	35	MG	35	HFS(5)	Average	338-2550	IL	312-368-7800
2	16.2	13.6	13.7	11.0		Low	6	26	LG	36	Home Depot(5)	Average	338-2550	IL	312-368-7800
ot rated						Average	7	25	MV	–3	Jardine Matheson Holdings(3)		338-2550	IL	312-368-7800
4	16.4	14.3				Average	23	19	LB	34	FNMA(3)	Low	338-2550	IL	312-368-7800
1	16.1	14.1	14.7	11.4		Average	5	24	MB	31	Allstate(4)	Average	338-2550	IL	312-368-7800
6	13.1	10.6	10.8	7.7		Average	5	18	LB	21	General Electric(2)	Low	338-2550	IL	312-368-7800
2						High	4	20	LB	15	General Electric(2)		428-6970		
ot rated						High	7	19	LB	14	Bristol-Myers Squibb(2)		428-6970		
8	11.5	9.4	9.6	7.0		Average	17	17	LV	19	DuPont(2)	Very low	245-5040	PA	412-288-1900
7	11.5	9.2	8.7	5.8		Average	3	15	MV	–9	Delmarva Power & Light(5)	Low	634-5726	PA	610-941-0255

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK V OBJEC
STRONG AMERICAN UTILITIES		Utilities	118.2	212	No load	0.50	37.0	35.9	2.6	1
STRONG ASSET ALLOCATION (fff)	♦	Asset allocation	268.6	8	No load	1.20	22.0	18.6	3.9	23
STRONG COMMON STOCK	♦♦♦	Small company	1061.0	34	No load‡	1.30	32.4	28.4	0.5	42
STRONG DISCOVERY	♦	Maximum growth	599.1	54	No load	1.50	34.8	31.0	0.5	22
STRONG GROWTH		Growth	642.8	506	No load	1.60	41.0	39.8	0.2	21/2
STRONG INTERNATIONAL STOCK		Foreign	214.7	–17	No load	1.70	7.8	7.0	2.7	45
STRONG OPPORTUNITY	♦♦	Growth	1327.7	65	No load	1.40	27.3	25.4	0.6	177/2
STRONG SCHAFER VALUE (ggg)	♦♦	Growth	180.6	152	No load	1.48	34.1	32.7	0.9	100/2
STRONG TOTAL RETURN	AVG	Growth/income	709.0	17	No load	1.20	27.0	25.1	1.2	119/1
SUNAMERICA BALANCED ASSETS B	AVG	Balanced	169.0	–3	4.00**	2.12†	27.0	24.4	1.3	19
SUNAMERICA SMALL COMPANY GRTH. A	♦♦	Small company	98.1	135	5.75	1.57†	50.2	43.0	0.0	10
TCW/DW BALANCED		Balanced	102.2	–19	No load	2.11†	22.1	21.8	0.9	48
TCW/DW CORE EQUITY		Growth	758.0	11	5.00**	1.96†	24.5	24.5	0.0	204/2
TCW/DW LATIN AMERICAN GROWTH		Foreign	234.1	–33	5.00**	2.87†	–20.3	–20.3	0.0	64
TCW/DW SMALL CAP GROWTH		Small company	132.7	99	5.00**	2.57†	60.2	60.2	0.0	3
TEMPLETON DEVELOPING MARKETS I		Emerging markets	2148.2	7	5.75	2.11†	0.4	–0.6	1.5	
TEMPLETON FOREIGN I	♦	Foreign	7312.5	38	5.75	1.15†	11.2	9.1	2.6	28
TEMPLETON GLOBAL OPPORT. I	♦	World	510.6	7	5.75	1.53†	12.8	10.9	1.5	27
TEMPLETON GROWTH I	AVG	World	7307.7	33	5.75	1.12†	18.4	15.1	2.3	13
TEMPLETON REAL ESTATE SECS. I	♦	Real estate	124.6	–3	5.75	1.55†	6.0	5.1	2.9	
TEMPLETON SMALLER COMPANY GRTH. I	AVG	World	1407.2	10	5.75	1.36†	17.7	13.3	1.4	16
TEMPLETON WORLD I	AVG	World	5987.9	19	5.75	1.05†	21.6	17.0	2.2	6
THIRD AVENUE VALUE	♦♦♦	Growth	328.6	82	No load	1.16	31.7	30.7	1.8	129/2
TOWER CAPITAL APPRECIATION	AVG	Growth/income	154.8	21	3.00	1.25	37.7	35.4	1.1	7/1
TWEEDY BROWNE AMERICAN VALUE		Growth	163.7	429	No load	1.74	36.2	35.8	0.8	62/2
TWEEDY BROWNE GLOBAL VALUE		World	794.0	43	No load	1.65	10.7	10.2	0.0	31
TWENTIETH CENTURY BALANCED INV.	♦	Balanced	839.8	22	No load	0.98	21.4	18.5	2.7	52
TWENTIETH CENTURY EQUITY-INCOME		Equity-income	96.8	306	No load	1.00	29.6	25.8	3.1	17
TWENTIETH CENTURY GIFTRUST INV.	AVG	Small company	603.2	120	No load	0.98	38.3	35.2	0.0	26
TWENTIETH CENTURY GROWTH INV.	♦♦	Growth	4849.0	17	No load	1.00	20.3	15.7	0.3	223/2
TWENTIETH CENTURY HERITAGE INV.	♦	Growth	1026.1	20	No load	0.99	26.7	24.7	0.4	188/2
TWENTIETH CENTURY INTL. EMERGING GRTH.		Foreign	121.2	8	2.00*	2.00	9.9	9.7	0.5	32
TWENTIETH CENTURY INTL. EQUITY		Foreign	1258.4	–1	No load	1.84	11.9	11.9	0.1	20
TWENTIETH CENTURY SELECT INV.	♦♦	Growth	3982.8	0	No load	1.00	22.7	18.5	0.7	213/2
TWENTIETH CENTURY ULTRA INV.	♦♦	Maximum growth	14551.2	48	No load	1.00	37.7	35.9	0.0	10
TWENTIETH CENTURY VALUE		Growth/income	652.5	326	No load	1.00	32.8	29.2	2.1	61/1
TWENTIETH CENTURY VISTA INV.	♦♦	Small company	1774.6	116	No load	0.98	46.1	43.5	0.0	16
UNITED ACCUMULATIVE A	AVG	Growth	1206.3	25	5.75	0.71	34.5	30.0	1.2	92/2
UNITED CONTINENTAL INCOME A	♦	Balanced	493.2	18	5.75	0.89†	24.8	22.4	2.8	36
UNITED INCOME A	AVG	Equity-income	3974.4	26	5.75	0.74†	29.7	28.1	1.2	16
UNITED INTERNATIONAL GROWTH A	♦♦	Foreign	701.4	10	5.75	1.25†	8.1	5.8	0.7	42
UNITED NEW CONCEPTS A	♦♦	Small company	450.2	65	5.75	1.24†	34.1	33.0	0.2	35
UNITED RETIREMENT SHARES A	♦	Balanced	576.4	22	5.75	0.89†	24.4	21.5	2.8	37
UNITED SCIENCE & TECHNOLOGY A	♦	Technology	827.5	67	5.75	0.96†	55.6	54.3	0.0	2
UNITED SERVICES GOLD SHARES	♦♦♦	Precious metals	175.4	–40	0.10*	1.42	–26.8	–27.5	3.1	15
UNITED SERVICES WORLD GOLD	♦♦♦	Precious metals	184.8	1	0.10*	1.55	15.9	15.9	0.0	1
UNITED VANGUARD A	♦	Growth	1257.7	24	5.75	1.05†	24.9	22.9	0.5	201/2
USAA AGGRESSIVE GROWTH	♦♦	Maximum growth	442.8	56	No load	0.86	50.4	47.9	0.0	2
USAA CORNERSTONE STRATEGY (hhh)	AVG	Multi-asset global	949.7	13	No load	1.13	18.4	16.9	3.0	12
USAA GOLD	♦♦♦	Precious metals	143.3	–10	No load	1.28	4.0	4.0	0.1	7
USAA GROWTH	AVG	Growth	1067.8	58	No load	1.04	32.1	29.7	1.5	125/2
USAA GROWTH & INCOME		Growth/income	267.3	78	No load	1.01	31.6	30.5	1.8	74/1
USAA GROWTH & TAX STRATEGY (iii)	♦	Balanced	149.3	20	No load	0.80	22.7	21.2	3.7	46
USAA INCOME	♦♦	Asset allocation	1893.2	17	No load	0.41	24.5	22.1	6.5	15
USAA INCOME STOCK	♦	Equity-income	1585.5	35	No load	0.75	28.6	26.1	4.8	19
USAA INTERNATIONAL	♦♦	Foreign	351.4	4	No load	1.17	8.3	8.0	0.4	40
USAA WORLD GROWTH		World	223.6	21	No load	1.28	12.8	12.1	0.6	26
VALUE LINE	♦	Growth	317.6	16	No load	0.82	32.1	29.5	0.7	124/2
VALUE LINE INCOME	AVG	Equity-income	144.3	10	No load	0.90	26.2	24.1	3.3	25
VALUE LINE LEVERAGED GROWTH INV.	♦	Maximum growth	337.3	27	No load	0.89	37.1	33.1	0.3	13
VALUE LINE SPECIAL SITUATIONS	♦♦	Maximum growth	98.4	9	No load	1.10	29.0	21.1	0.3	28
VAN ECK GOLD/RESOURCES A	♦♦♦	Precious metals	156.1	–17	5.75	1.52†	4.3	4.3	0.0	6
VAN ECK INTL INVESTORS GOLD A	♦♦♦	Precious metals	509.5	–20	5.75	1.15	–8.9	–9.9	0.8	14
VAN KAMPEN AMER. CAP COMSTOCK A (jjj)	AVG	Growth/income	1078.2	24	5.75	1.01†	36.2	30.9	1.6	29/1
VAN KAMPEN AMER. CAP EMRG. GRTH. A (kkk)	♦	Small company	1153.6	70	6.75*	1.18†	44.6	40.8	0.0	18
VAN KAMPEN AMER. CAP ENTERPRISE A (lll)	AVG	Growth	1025.2	37	5.75	1.05†	33.9	28.5	0.5	102/2
VAN KAMPEN AMER. CAP EQUITY-INC B (mmm)		Equity-income	409.3	69	5.00**	1.82†	31.5	28.9	2.2	13
VAN KAMPEN AMER. CAP GR. & INC. A (nnn)	♦	Growth/income	399.2	94	5.75	1.38†	35.7	32.7	1.8	33/1
VAN KAMPEN AMER. CAP PACE A (ooo)	♦	Growth	2428.4	18	5.75	1.04†	32.8	27.3	1.2	116/2
VAN KAMPEN AMER. CAP UTILITY B (ppp)		Utilities	100.1	27	4.00**	2.06†	24.4	23.2	3.3	21

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not mea (fff) Formerly Strong Investment. (ggg) Formerly Schafer Value. (hhh) Formerly USAA Cornerstone. (iii) Formerly USAA Balanced. (jjj) Formerly American Capital Comstock A. (kkk) ly American Capital Emerging Growth A. (lll) Formerly American Capital Enterprise A. (mmm) Formerly American Capital Equity-Income B. (nnn) Formerly American Capital Growth & A.(ooo) Formerly American Capital Pace A. (ppp) Formerly Van Kampen Merritt Utility B.

E ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
ARS	5 YEARS		10 YEARS		BW 10-YEAR	TURNOVER	%CASH	P-E	STYLE	UNTAXED	LARGEST HOLDING		TOLL-FREE	IN-STATE	
TERTAX	PRETAX	AFTERTAX	PRETAX	AFTERTAX	ANALYSIS			RATIO		GAINS (%)	COMPANY (% ASSETS)		(800)		
, not rated						High	12	17	LV	10	Ameritech(10)		368-1030	WI	414-359-1400
8.6	11.2	8.6	9.5	6.4		Very high	4	27	MG	11	Intergroup(2)	Very low	368-1030	WI	414-359-1400
15.7	25.6	22.6				Average	12	23	MB	23	Cirrus Logic(2)	Average	368-1030	WI	414-359-1400
13.0	21.6	17.9				Very high	5	32	MG	17	IBM(5)	High	368-1030	WI	414-359-1400
, not rated						Very high	7	36	MG	16	Just For Feet(2)		368-1030	WI	414-359-1400
14.5						High	5	23	MV	–3	Sensonor(2)		368-1030	WI	414-359-1400
15.0	19.7	18.5	18.3	16.7		Average	13	23	MB	18	Paging Network(1)	Average	368-1030	WI	414-359-1400
15.4	21.6	18.8	14.9	12.8		Low	6	19	MV	14	Mellon Bank(3)	Average	368-1030	WI	414-359-1400
14.4	15.6	14.9	11.2	8.8		Very high	6	26	LG	17	Medtronic(2)	Average	368-1030	WI	414-359-1400
9.6	13.6	10.6	10.5	8.2		High	5	22	LB	15	Woolworth(2)	Low	858-8850	NY	212-551-5353
18.3	27.2	24.6				Very high	11	37	SG	35	PC DOCS Group International(2)	Average	858-8850	NY	212-551-5353
, not rated						High	4	20	LV	9	Unisys(3)		526-3143	NY	212-392-2550
11.0						Average	0	21	LB	28	National Semiconductor(4)		526-3143	NY	212-392-2550
-4.1						High	1	27	MG	–62	Telefonos de Mexico L (ADR)(7)		526-3143	NY	212-392-2550
, not rated						High	8	44	SG	29	Maxim Integrated Products(2)		526-3143	NY	212-392-2550
16.0						Low	19	14	MV	2	Cheung Kong Holdings(3)		292-9293	FL	813-823-8712
13.3	12.6	10.5	16.2	13.7		Low	19	14	LV	4	HSBC Holdings (HK)(2)	Average	292-9293	FL	813-823-8712
11.8	16.3	14.1				Average	2	15	MV	14	Peregrine Investments Hldgs(2)	Average	292-9293	FL	813-823-8712
13.7	16.7	13.7	14.1	11.2		Low	20	15	LV	12	Merrill Lynch(2)	Average	292-9293	FL	813-823-8712
8.5	12.7	11.8				Average	8	19	SV	–6	Patten(3)	Average	292-9293	FL	813-823-8712
12.1	16.4	13.3	11.2	7.9		Low	25	17	SB	19	News International(3)	Average	292-9293	FL	813-823-8712
14.1	17.0	13.3	12.7	9.2		Low	12	15	LV	14	Merrill Lynch(3)	Average	292-9293	FL	813-823-8712
16.2	21.2	19.4				Very low	20	17	SV	20	Eljer Industries(5)	Low	443-1021	NY	212-888-6685
13.2	15.1	12.7				Average	2	18	LB	27	General Electric(2)	Average	999-0124	PA	504-587-2708
, not rated						Very low	18	20	MV	13	American Express(4)		432-4789		
, not rated						Very low	12	22	MV	3	Unilever(3)		432-4789		
17.5	12.4	11.1				Average	7	26	LG	19	Hewlett-Packard(2)	Average	345-2021	MO	816-531-5575
, not rated							3	18	MV	10	Allied-Lyons(4)		345-2021	MO	816-531-5575
24.5	35.1	32.3	24.1	21.5		High	4	36	SG	38	Tencor Instruments(4)	Very high	345-2021	MO	816-531-5575
13.2	14.8	12.1	14.2	11.0		High	2	28	LG	29	Cisco Systems(3)	High	345-2021	MO	816-531-5575
10.9	16.4	14.8				High	2	25	MB	24	Micron Technology(3)	High	345-2021	MO	816-531-5575
, not rated							1	26	SG	5	Bang & Olufsen Holding Cl B(3)		345-2021	MO	816-531-5575
13.9						Very high	2	31	MB	8	Mannesmann (Germany)(4)		345-2021	MO	816-531-5575
15.7	10.2	7.6	11.8	9.0		High	4	21	LV	27	IBM(5)	High	345-2021	MO	816-531-5575
16.5	25.0	24.5	19.8	17.9		High	1	31	LG	40	3Com(4)	Very high	345-2021	MO	816-531-5575
, not rated						High	3	21	MV	10	Allied-Lyons(3)		345-2021	MO	816-531-5575
15.0	22.4	20.5	17.0	15.4		High	2	36	MG	40	LSI Logic(6)	Very high	345-2021	MO	816-531-5575
10.2	15.7	12.8	13.1	9.1		Very high	6	22	LB	16	ITT(3)	Average	366-5465	KS	913-236-2000
10.2	14.4	12.7	10.8	8.2		Average	5	20	LV	17	ITT(3)	Low	366-5465	KS	913-236-2000
12.7	16.2	15.0	14.9	12.2		Low	3	21	LB	42	Motorola(3)	Average	366-5465	KS	913-236-2000
14.7	13.6	11.9	12.0	9.3		Average	2	18	MB	18	Nokia Cl K(7)	High	366-5465	KS	913-236-2000
16.9	26.6	25.7	15.3	13.7		Average	23	35	MG	39	America Online(5)	Average	366-5465	KS	913-236-2000
9.7	13.9	11.9	11.9	9.2		Average	6	19	LB	22	Chubb(3)	Very low	366-5465	KS	913-236-2000
21.0	23.1	21.6	17.6	15.1		Average	8	35	MG	45	Ascend Communications(5)	High	366-5465	KS	913-236-2000
16.0	–7.9	–8.7	–1.8	–3.3		Low	–17	31		–106	Free State Consld Gold (ADR)(10)	Very high	873-8637	TX	210-308-1222
12.2	11.0	11.0	7.6	7.1		Low	–1	38	SG	–6	Barrick Gold(12)	Very high	873-8637	TX	210-308-1222
13.1	14.8	13.4	12.8	9.9		Average	13	27	LG	35	Nokia Cl K(4)	Average	366-5465	KS	913-236-2000
15.1	20.4	18.5	12.0	9.9		High	4	39	SG	32	HBO(2)	Very high	382-8722		
11.3	12.4	10.8	12.7	11.3		Low	1	23	MB	12	Boeing(1)	Low	382-8722		
14.3	5.6	5.5	5.5	5.0		Low	3	40	MG	–71	Barrick Gold(9)	Very high	382-8722		
10.1	15.6	13.0	12.5	9.7		Average	5	20	LB	10	Philip Morris(5)	Average	382-8722		
, not rated						Low	5	21	LB	14	Boeing(3)		382-8722		
9.0	10.3	8.7				Very high	3	21	LV	11	Boeing(3)	Very low	382-8722		
16.6	10.9	8.4	10.4	7.2		Low	2	14	MV	3	Allegheny Power System(2)	Very low	382-8722		
10.3	14.4	12.2				Low	4	18	LV	9	Bristol-Myers Squibb(5)	Low	382-8722		
14.9	12.0	11.3				Average	3	23	MB	7	Heineken (Netherlands)(2)	High	382-8722		
11.6						Average	3	23	LB	11	Boeing(1)		382-8722		
17.3	16.6	13.2	14.2	10.8		High	5	24	MB	28	XTRA(1)	High	223-0818	NY	212-907-1500
16.7	11.3	8.9	10.6	7.4		Average	9	20	LV	14	Texaco Capital(2)	Low	223-0818	NY	212-907-1500
13.5	17.0	14.1	14.4	11.3		Average	2	22	MG	44	Deere(2)	High	223-0818	NY	212-907-1500
10.4	14.4	11.9	8.5	6.5		Average	47	27	SG	47	Caremark International(1)	Very high	223-0818	NY	212-907-1500
16.7	7.5	7.5				Very low	–1	40	MG	–43	Barrick Gold(13)	Very high	826-1115	NY	212-687-5200
13.0	6.9	5.9	8.1	6.6		Very low	4	43	MG	31	Barrick Gold(7)	Very high	826-1115	NY	212-687-5200
17.5	15.0	10.9	12.6	8.9		High	6	19	LV	20	Philip Morris(3)	Average	421-5666		
16.5	24.0	21.8	15.8	13.6		Average	14	31	MG	33	S&P 500 Futures December(3)	High	421-5666		
10.5	17.5	13.8	13.5	9.4		Very high	6	20	LB	27	Intel(3)	Average	421-5666		
11.8						High	8	20	LB	15	IBM(2)		421-5666		
12.3	17.2	14.3	12.6	9.6		Very high	7	22	LB	4	Royal Dutch Petroleum (ADR)(2)	Low	421-5666		
18.0	14.2	10.4	11.5	8.1		Very high	7	21	LB	24	American Cap Small Cap(2)	Average	421-5666		
, not rated							3	17	MV	–2	NYNEX(3)		421-5666		

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1995 RETURNS (%)			
			ASSETS $MIL.	% CHG. 1994-5	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK W OBJEC
VANGUARD ASSET ALLOCATION	▲▲	Asset allocation	1791.0	59	No load	0.49	35.5	32.7	3.7	2/
VANGUARD BALANCED INDEX		Balanced	590.1	46	No load	0.20	28.6	27.1	3.5	11/
VANGUARD EQUITY-INCOME	▲▲	Equity-income	1102.8	28	No load	0.45	37.3	35.5	3.6	1/
VANGUARD EXPLORER	▲	Small company	1647.6	47	No load	0.70	26.6	23.8	0.4	64/
VANGUARD INDEX 500	▲	Growth/income	17371.8	86	No load	0.19	37.4	36.5	2.1	10/1
VANGUARD INDEX EXTENDED MARKET	▲	Small company	1523.2	57	No load	0.20	33.8	32.7	1.2	37/
VANGUARD INDEX GROWTH		Growth	271.0	214	No load	0.20	38.1	37.5	1.4	43/2
VANGUARD INDEX SMALL CAP STOCK	▲	Small company	971.2	60	No load	0.17	28.7	27.4	1.2	56/
VANGUARD INDEX TOTAL STOCK MKT.		Growth/income	1570.9	100	No load	0.20	35.8	34.8	1.9	32/1
VANGUARD INDEX VALUE		Growth/income	496.3	67	No load	0.20	37.0	35.9	2.7	14/1
VANGUARD INTL. EQUITY EMERG MKTS.		Emerging markets	234.3	181	1.00*	0.60	0.5	–0.1	1.7	
VANGUARD INTL. EQUITY EUROPEAN	▼▼	Europe	1017.3	42	No load	0.32	22.3	21.3	2.3	2/
VANGUARD INTL. EQUITY PACIFIC	▼▼▼	Pacific	830.7	19	No load	0.32	2.8	2.5	1.0	14/
VANGUARD INTL. GROWTH	▼▼	Foreign	3676.4	26	No load	0.58	14.9	14.0	1.3	11/
VANGUARD LIFESTRAT CONSERV. GRTH.		Asset allocation	219.3	431	No load	0.00	24.3	22.5	4.0	16/
VANGUARD LIFESTRAT GROWTH		Asset allocation	217.4	476	No load	0.00	29.2	27.8	2.5	5/
VANGUARD LIFESTRAT INCOME		Asset allocation	120.7	950	No load	0.00	23.0	21.2	4.2	21/
VANGUARD LIFESTRAT MODERATE GRTH.		Asset allocation	234.7	574	No load	0.00	27.9	26.4	2.9	9/
VANGUARD PREFERRED STOCK	▲▲	Equity-income	311.4	12	No load	0.52	25.9	23.3	7.0	26/
VANGUARD QUANTITATIVE	AVG	Growth/income	909.4	53	No load	0.48	35.9	33.7	2.0	31/1
VANGUARD SPECIAL ENERGY	▼▼▼	Natural resources	506.4	14	1.00*	0.30	25.3	24.1	1.6	4/
VANGUARD SPECIAL GOLD & PREC. MET.	▼▼▼	Precious metals	549.5	–14	1.00*	0.25	–4.5	–4.9	1.4	13/
VANGUARD SPECIAL HEALTH CARE	AVG	Health care	1473.4	108	1.00*	0.40	45.2	43.9	1.1	
VANGUARD SPECIAL UTILITIES INC.		Utilities	757.7	35	No load	0.50	34.0	32.2	4.4	4/
VANGUARD STAR	▲▲	Balanced	4841.8	29	No load	0.00	28.7	25.9	3.8	10/
VANGUARD TAX-MANAGED CAP APPREC.		Growth	254.2	265	2.00*	0.20	34.4	34.1	0.7	95/2
VANGUARD TAX-MANAGED GRTH. & INC.		Growth/income	98.3	213	2.00*	0.20	37.5	36.7	1.9	8/1
VANGUARD U.S. GROWTH	AVG	Growth	3624.1	72	No load	0.44	38.4	36.8	1.4	36/2
VANGUARD/MORGAN GROWTH	AVG	Growth	1471.1	37	No load	0.50	36.0	32.7	1.0	67/2
VANGUARD/PRIMECAP	AVG	Growth	3236.8	111	No load‡	0.64	35.5	34.3	0.8	77/2
VANGUARD/TRUSTEES' EQUITY INTL.	▼▼	Foreign	988.1	–6	No load	0.34	9.6	6.6	2.3	35/
VANGUARD/TRUSTEES' EQUITY U.S.	AVG	Growth/income	137.5	22	No load	0.73	33.2	31.5	1.6	55/1
VANGUARD/WELLESLEY INCOME	▲▲	Balanced	7180.7	26	No load	0.34	28.9	26.3	5.5	9/
VANGUARD/WELLINGTON	▲▲	Balanced	12656.0	44	No load	0.35	32.9	30.9	3.9	2/
VANGUARD/WINDSOR	▲	Growth/income	13646.3	28	No load‡	0.45	30.1	25.9	2.9	93/1
VANGUARD/WINDSOR II	▲	Growth/income	11013.0	38	No load	0.39	38.8	36.5	2.7	4/1
VICTORY BALANCED		Balanced	217.3	39	4.75	0.87	26.1	24.5	3.6	25/
VICTORY DIVERSIFIED	AVG	Growth	442.8	71	4.75	0.89	35.4	31.8	1.7	78/2
VICTORY GROWTH		Growth	111.9	85	4.75	0.94	31.5	29.7	0.9	132/2
VICTORY INTERNATIONAL GROWTH	▼▼	Foreign	105.3	32	4.75	1.48	7.7	7.7	0.0	46/
VICTORY SPECIAL VALUE		Growth	208.0	72	4.75	1.00	26.8	25.4	1.2	187/2
VICTORY STOCK INDEX		Growth/income	178.0	90	4.75	0.58	36.5	35.0	2.1	23/1
VICTORY VALUE		Growth	318.5	71	4.75	0.92	33.7	31.9	2.1	106/2
VISTA CAPITAL GROWTH A	AVG	Growth	724.2	33	4.75	1.49†	22.2	20.8	0.5	215/2
VISTA GROWTH & INCOME A	▲▲	Growth/income	1501.0	12	4.75	1.40†	27.6	25.2	1.7	116/1
VONTOBEL EUROPACIFIC	▼▼	Foreign	129.2	–7	No load	1.54	10.9	9.4	1.0	29/
WADDELL & REED GROWTH B		Growth	174.4	116	3.00**	2.23†	32.2	31.6	0.0	122/2
WADDELL & REED TOTAL RETURN B		Growth/income	166.7	79	3.00**	2.05†	29.7	29.6	0.0	100/1
WARBURG PINCUS CAPTL. APPR. COMM.	AVG	Growth	256.0	76	No load	1.05	38.1	33.5	0.3	42/2
WARBURG PINCUS EMERG. GROWTH COMM.	AVG	Small company	557.1	150	No load	1.22	46.3	44.0	0.0	15/
WARBURG PINCUS GROWTH & INC. COMM.	AVG	Growth	985.3	57	No load	1.22	20.4	18.2	1.3	222/2
WARBURG PINCUS INTL. EQUITY COMM.	▼▼	Foreign	2220.9	43	No load	1.44	10.4	9.3	3.2	30/
WARBURG PINCUS JAPAN OTC COMM.		Pacific	212.0	851	1.00*	1.00†	–1.1	–2.3	4.2	18/
WASATCH AGGRESSIVE EQUITY	AVG	Maximum growth	294.0	430	No load‡	1.47	28.1	27.3	0.0	29/
WASATCH MID-CAP		Growth	130.5	NM	No load	1.75	58.8	58.3	0.0	1/2
WASHINGTON MUTUAL INVESTORS	▲	Growth/income	18786.1	48	5.75	0.69†	41.2	38.2	2.7	1/1
WAYNE HUMMER GROWTH	AVG	Growth	100.2	14	No load	1.07	24.8	23.7	1.2	203/2
WEITZ VALUE	▲▲	Growth	149.4	39	No load	1.42	38.4	35.3	2.2	35/2
WILLIAM BLAIR GROWTH SHARES	▲	Growth	362.4	99	No load	0.71	29.1	27.7	0.2	154/2
WINTHROP FOCUS AGGRESSIVE GROWTH	▲▲▲	Maximum growth	214.2	45	4.00**	1.70†	20.2	19.3	0.2	31/
WINTHROP FOCUS GROWTH & INCOME	AVG	Growth/income	96.6	46	4.00**	1.64†	29.5	28.1	1.6	101/1
WOODWARD OPPORTUNITY RET.		Small company	650.5	30	5.00	0.90†	19.8	18.1	0.4	83/
WPG QUANTITATIVE EQUITY		Growth/income	120.2	84	No load	1.14	33.4	33.3	0.1	53/1
WPG TUDOR	▼▼	Growth	163.4	3	No load	1.28	41.2	39.7	0.0	18/2
WRIGHT INTL. BLUE CHIP EQUITIES	▼▼	Foreign	237.3	18	No load	1.31†	13.6	13.4	0.7	13/
WRIGHT SELECTED BLUE CHIP EQUITY	AVG	Growth/income	217.6	16	No load	1.03†	30.3	27.9	1.1	88/1
YACKTMAN		Growth	566.7	92	No load	1.07†	30.4	27.5	1.7	142/2
ZWEIG APPRECIATION A		Small company	272.7	28	5.50	1.70†	24.0	22.2	2.0	71/
ZWEIG MANAGED ASSETS C		Multi-asset global	527.3	–8	1.25**	2.38†	15.4	12.8	4.8	14/
ZWEIG STRATEGY A	AVG	Growth	558.2	31	5.50	1.40†	25.1	22.9	2.5	200/2

*Includes redemption fee. **Includes deferred sale. charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts. §Less than 0.5% of assets. NA=Not available. NM=Not me

ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE		
S RTAX	5 YEARS PRETAX	5 YEARS AFTERTAX	10 YEARS PRETAX	10 YEARS AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)		IN-STATE
2.5	15.2	13.2				Low	2	20	LB	20	General Electric(1)	Low	662-7447	PA	610-669-1000
0.4						Low	1	21	LB	15	General Electric(1)		662-7447	PA	610-669-1000
3.7	16.2	14.3				Low	6	18	LV	27	Philip Morris(3)	Low	662-7447	PA	610-669-1000
1.2	21.0	19.1	10.5	8.7		Average	11	25	SB	21	Dionex(1)	Average	662-7447	PA	610-669-1000
4.2	16.4	15.4	14.6	13.0		Very low	1	20	LB	26	General Electric(3)	Average	662-7447	PA	610-669-1000
3.7	19.1	18.2				Low	3	23	MB	29	Berkshire Hathaway(2)	Average	662-7447	PA	610-669-1000
2.3						Low	0	23	LG	18	General Electric(5)		662-7447	PA	610-669-1000
3.5	21.2	19.8	10.6	8.6		Low	2	23	SB	20	Nellcor Puritan Bennett()	Average	662-7447	PA	610-669-1000
3.6						Very low	2	21	LB	20	General Electric(2)		662-7447	PA	610-669-1000
5.9						Low	0	17	LV	17	Exxon(4)		662-7447	PA	610-669-1000
not rated							5	22	LG	–7	Telekom Malaysia(3)		662-7447	PA	610-669-1000
6.4	11.8	11.0				Very low	2	20	LB	21	Royal Dutch Petroleum (Neth)(3)	High	662-7447	PA	610-669-1000
5.9	7.4	7.0				Very low	1	42	LG	6	Toyota Motor(3)	Very high	662-7447	PA	610-669-1000
8.2	10.6	9.9	13.6	11.5		Low	3	25	LB	19	Ito-Yokado(3)	High	662-7447	PA	610-669-1000
not rated							1	21	LB	9	Vanguard Asset Allocation(30)		662-7447	PA	610-669-1000
not rated							1	22	LB	11	Vanguard Index Total Stk Mkt(45)		662-7447	PA	610-669-1000
not rated							0	20	LB	8	Vanguard F/I Short-Trm Corp(32)		662-7447	PA	610-669-1000
not rated							0	22	LB	10	Vanguard Index Total Stk Mkt(35)		662-7447	PA	610-669-1000
6.9	11.4	8.8	10.4	7.4		Low	3	NA		0	NA()	Very low	662-7447	PA	610-669-1000
3.0	16.5	14.2				Average	6	18	LV	24	Exxon(3)	Average	662-7447	PA	610-669-1000
4.1	10.7	8.9	13.0	10.6		Very low	3	32	MG	4	Exxon(5)	Very high	662-7447	PA	610-669-1000
9.8	8.0	7.3	10.6	9.3		Very low	8	35	MG	1	Euro-Nevada Mining(3)	Very high	662-7447	PA	610-669-1000
19.1	20.7	18.9	20.0	17.7		Low	11	25	MG	30	Pfizer(5)	Average	662-7447	PA	610-669-1000
10.0						Low	5	16	MV	5	GTE(4)		662-7447	PA	610-669-1000
10.4	14.3	12.2	11.9	8.9		Very low	13	18	LV	18	Vanguard/Windsor II(40)	Very low	662-7447	PA	610-669-1000
, not rated							0	24	LB	15	General Electric(2)		662-7447	PA	610-669-1000
, not rated							0	20	LB	15	General Electric(3)		662-7447	PA	610-669-1000
11.6	16.4	15.7	13.0	10.8		Low	5	24	LG	30	PepsiCo(5)	Average	662-7447	PA	610-669-1000
10.2	15.2	12.8	13.0	9.4		Average	9	22	LB	31	Hewlett-Packard(2)	Average	662-7447	PA	610-669-1000
20.2	20.9	19.7	15.5	14.3		Very low	11	22	MB	31	Federal Express(5)	Average	662-7447	PA	610-669-1000
12.8	8.6	7.0	14.0	10.1		Average	4	23	MV	19	Onward Kashiyama(2)	High	662-7447	PA	610-669-1000
13.0	15.1	13.7	12.2	9.2		High	3	18	LB	26	Philip Morris(2)	Average	662-7447	PA	610-669-1000
9.7	13.3	10.8	11.9	8.9		Low	2	16	LV	10	CoreStates Financial(2)	Very low	662-7447	PA	610-669-1000
12.7	14.9	13.0	12.8	10.3		Low	2	17	LV	23	General Electric(2)	Low	662-7447	PA	610-669-1000
12.5	18.4	15.2	13.5	9.4		Low	18	13	LV	19	Chrysler(6)	Average	662-7447	PA	610-669-1000
13.9	17.6	15.6	14.4	11.9		Low	6	16	LV	23	Anheuser-Busch(3)	Low	662-7447	PA	610-669-1000
d, not rated							7	17	LV	9	Shearson US Treasury Fund(3)		539-3863		
12.0	16.0	13.2				High	0	19	LB	17	Chevron(4)	Average	539-3863		
d, not rated							5	21	LG	15	Microsoft(4)		539-3863		
14.0	9.1	8.5				Average	2	29	LB	4	Japan Associated Finance(2)	High	539-3863		
d, not rated							7	19	MV	14	Michigan National(3)		539-3863		
d, not rated							15	20	LB	17	AT&T(2)		539-3863		
d, not rated							6	18	LV	14	Texaco(3)		539-3863		
12.2	22.8	22.1				Average	10	19	MV	13	AGCO(2)	Average	648-4782		
10.5	20.6	19.1				Average	14	17	LV	17	Kroger(1)	Average	648-4782		
13.3	11.4	11.0	6.9	6.7		Low	5	26	LB	24	Roche Holding (Gen)(3)	Average	527-9500		
22.1						Average	27	31	SG	26	H&R Block(2)			KS	913-236-2000
13.1						Low	6	21	LB	19	Motorola(3)			KS	913-236-2000
12.9	16.2	13.9				Average	4	24	MB	29	Kimberly-Clark(5)	Average	257-5614	NY	212-878-0600
18.2	24.4	23.4				Average	6	35	SG	30	Maxim Integrated Products(3)	High	257-5614	NY	212-878-0600
17.4	17.0	14.4				High	13	24	MB	8	First Interstate Bancorp(5)	Average	257-5614	NY	212-878-0600
17.9	14.0	13.3				Low	5	25	LV	3	East Japan Railway()	High	257-5614	NY	212-878-0600
d, not rated							11	47		–5	Seikagaku(5)		257-5614	NY	212-878-0600
16.8	21.3	19.6				Low	3	26	SB	16	Century Tel Enterprises(5)	High	551-1700	UT	801-533-0777
18.4						Average	11	32	SG	9	Hummingbird Communications(7)		551-1700	UT	801-533-0777
15.0	16.7	14.7	14.6	12.3		Low	5	18	LB	32	Pacific Telesis Group(2)	Low	421-4120	DC	202-842-5665
7.8	12.7	11.9	12.2	10.8		Very low	8	21	MB	30	Avery Dennison(4)	Low	621-4477	IL	312-431-1700
12.7	16.8	15.0				Low	3	19	MV	22	Countrywide Credit Industry(5)	Low	232-4161	NE	402-391-1980
14.4	19.8	17.5	14.9	10.8		Average	6	30	MG	28	Home Depot(3)	Average	742-7272		
11.8	21.0	18.3	12.6	9.4		Low	3	18	SV	5	Teleflex(3)	Low	225-8011	NY	212-504-4000
11.9	13.9	11.8	11.2	8.1		Low	4	22	LB	22	Amoco(4)	Low	225-8011	NY	212-504-4000
11.3						Average	3	20	SV	15	FINOVA Group(2)		688-3350	MI	313-259-0729
14.5						Average	–1	21	LB	18	Exxon(5)		223-3332	NY	212-908-9582
9.9	17.2	14.7	13.1	9.8		High	0	33	SG	33	Informix(3)	Very high	223-3332	NY	212-908-9582
12.5	10.0	9.8				Very low	1	19	MB	16	Douglas Holding(1)	High	888-9471	CT	203-333-6666
7.5	12.9	10.5	11.6	8.9		Average	0	17	MV	21	BMC Industries(2)	Average	888-9471	CT	203-333-6666
8.5						Average	4	22	MG	14	Philip Morris(9)		525-8258	IL	312-201-1200
10.3						High	14	15	MV	21	Philips Electronics(1)		444-2706	NY	212-635-9800
nd, not rated						Very high	10	21	LB	6	Merck(1)		444-2706	NY	212-635-9800
10.2	14.1	11.9				Average	24	14	MV	17	Micron Technology(2)	Low	444-2706	NY	212-635-9800

DATA: MORNINGSTAR, INC., CHICAGO, IL.

Otis Carrier Pratt & Whitney Sikorsk

Companies seeking the fastest growth will find it in:

- new york
- north america
- *territories once regarded as alien*

Penang? Wuhan? Hanoi? As commercial centers, they were once right up there with the far side of the moon.

Today they're the future.

In the next five years, 85% of the growth in air conditioning will come from a 4,000-mile-wide band around the Equator. We're there. The elevator market in the People's Republic of China will double in that same time. We're there too. And by 2010 one-quarter of the world's jet engines will be made in the former Soviet Union. We were there first as well.

Because leading the way into a market often leads to market leadership.

Be there first.

Hamilton Standard UT Automotive

United Technologies

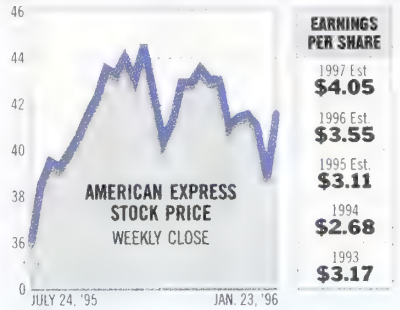
BY GENE G. MARCIAL

DON'T LEAVE YOUR BROKER WITHOUT IT?

Never mind that American Express (AXP) shares fell 1¼, to 41½, on Jan. 23, after the company posted disappointing yearend results. And don't fret, say some money pros, that analysts were quick to cut their 1996 and 1997 estimates. The stock, they argue, will be one of this year's biggest stars.

What's behind their bullishness? For one thing, they argue that AmEx, a travel and financial-services giant, is undervalued—selling at a price-earnings ratio of only 11, based on revised 1996 earning estimates. For another, there are recurring whispers that AmEx is a merger target.

A BID COULD DISPEL DOLDRUMS



DATA: BLOOMBERG FINANCIAL MARKETS, OPPENHEIMER & CO

The chief investment strategist of a New York investment bank insists that "AmEx is back on the buyout radar screen" of another huge financial-services company. He believes this suitor may offer $30 billion, or $60 a share, in a stock-and-cash merger deal.

This banker says AmEx would mesh well with the global outfit that's so interested in a deal. "A perfect strategic fit," he says. An AmEx spokeswoman declined comment.

AmEx' Travel Related Services markets travelers checks and the American Express Card. And American Express Bank serves customers through offices in 37 countries. AmEx Financial Advisors (formerly IDS Financial Services) provides insurance, mutual funds, and financial planning to individuals and businesses.

Says value investor Mark Boyar: "This company is one of the most undervalued components of the Dow Jones industrial average." Boyar, who heads a New York firm specializing in investments in companies with undervalued assets or franchises, says that, even without a merger, AmEx' stock price will hit 60 in a couple of years, based mainly on earnings-growth momentum and AmEx' broadening markets. With the Dow's 30 select corporations trading at 16 to 17 times their 1996 earnings estimates, AmEx could well trade at 15 to 16 times the 1996 estimate of $3.55—and get to the 55-60 range, says Boyar. As a measure of his confidence in AmEx, says Boyar, he has continued to buy shares.

Ned Davis of Oppenheimer, one of the analysts who have rolled back 1996 and 1997 estimates, still thinks that AmEx is a strong buy. He agrees that the p-e ratio is attractively low, considering AmEx has a "sustainable growth rate of 14%."

THIS STARTUP IS A REAL HEARTTHROB

Shares of Angeion (ANGN) have performed dramatically, rising from 5⅛ in mid-October to nearly 9 by Jan. 23. That's quite a feat for a little company that has yet to make a penny. And its rivals are giants in cardiovascular and neurological medical devices, where Angeion is still trying to gain a toehold. What's pushing up the stock?

Some savvy investors say that Angeion's chief product, the Sentinel implantable cardioverter-defibrillator (ICD), is the smallest and the most sophisticated such heartbeat-regulating device yet. The Food & Drug Administration apparently agrees. In one of its fastest approvals yet, the FDA authorized Angeion within 30 days to begin its human clinical tests.

Money manager Dennison Veru of Awad Associates says the stock will now be "event-driven," as Angeion moves to become a revenue-generating company. He expects two things to push up the stock: Initial U.S. human implants of an ICD will take place a few days into the trials, and Angeion will get approval to market the implantable ICD in Europe.

Another boost to Angeion bulls: St. Jude Medical, a large producer of pacemakers, which has a 5% stake, is eager to see the Sentinel marketed in Europe, where St. Jude has great marketing muscle. Veru says St. Jude has no ICD product of its own, and some pros speculate that it's eyeing Angeion as a takeover target "after the Sentinel clears the clinical hurdles."

Analyst Chris Sassouni of Raymond James & Associates says the first quarter of 1996 will be "the most momentous" in Angeion's history, "so we will be aggressive buyers of the stock at its current price."

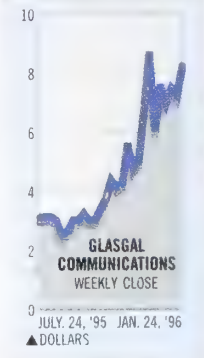
IBM AND EDS COULD BOTH MAKE OFFERS

In spite of the sell-off in technology stocks, not all members of that group are on the ropes. Even among obscure small-cap tech issues, there are a few winners. Glasgal Communications (GLAS) is one such: Its shares, trading at around 3 last summer, have rocketed to 8. And it doesn't even make computer gear. Glasgal is an "open systems" integrator: It designs, installs, and services networks that incorporate a broad range of hardware, networking systems, and software.

Demand in the integration business is mushrooming, says analyst John Duffy of Brookehill Equities. Glasgal helps small-to-midsize corporations that have multiple sites throughout the country—but no in-house network skill.

This growing market isn't served by such large outfits as Electronic Data Systems or Andersen Consulting. Because of Glasgal's dominant share in a niche market, EDS is rumored to be interested in acquiring it. One big investor is convinced that, once EDS makes a move on Glasgal, IBM may not be too far behind.

NETWORK DEMAND JUICES THE STOCK



DATA: BLOOMBERG FINANCIAL MARKETS

But no matter. Glasgal's business from its own clients is on the rise. Waterhouse Securities, one of its largest customers, is greatly expanding its network in 1996, according to Duffy. "This should result in additional revenues of $3 million to $4 million," he figures. Other big clients: Nynex and Bell Atlantic. Duffy thinks Glasgal will turn the corner this year and make money, vs. last year's loss of 15¢ a share. He expects earnings of 8¢ a share this year and 23¢ next. Glasgal thinks more big clients will sign on soon.

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SOFT DRINKS

WILL QUAKER GET THE RECIPE RIGHT?

It hopes to restore Snapple's zip with new ads and flavors

Quaker Oats Co. beverage honcho Donald R. Uzzi thought he was pitching a deal as sweet as Peach Snapple. Days after his company acquired Snapple Beverage Corp. at the end of 1994, Uzzi offered Snapple distributors the right to deliver the Gatorade sports drink. All they needed to do was turn over part of their exclusive Snapple territories to Gatorade's distribution system. The Snapple crowd's snappy answer: Keep your Gatorade. Quaker's tea party was off to a rocky start.

Quaker paid $1.7 billion for an iced-tea and fruit-drink brand that had used odd flavors and quirky ads to pioneer a new beverage category. The New Age drinks were supposed to provide earnings growth for the stagnant cereal maker and help it end perennial takeover rumors. But so far, Snapple has been more toxin than tonic.

BITTER BREW. First, those defiant independent Snapple distributors, armed with ironclad contracts, forced Quaker to scrap its plans to streamline distribution. Then, huge inventories of obsolete products and packaging overflowed into landfills and closeout stores. And where Snapple had once wooed a cult following with TV and radio ads featuring offbeat celebrities such as Howard Stern, Rush Limbaugh, and "Snapple Lady" Wendy Kaufman, Quaker didn't advertise the brand for months. Smelling blood, competitors such as PepsiCo Inc. and Coca-Cola Co. bored in with Lipton teas and Fruitopia juice drinks.

Profits predictably evaporated. Snapple lost $75 million in calendar 1995—when the soft-drink industry was basking in "the hottest friggin' summer on record," as analyst John M. McMillin of Prudential Securities Inc. puts it. For the quarter ended Dec. 31, its Chicago-based parent expects a loss of as muc as $60 million; Wall Street had forecast $7 million profit as recently as Decembe For this year, McMillin pegs Snapple operating earnings at around $40 mi lion. That's a substantial improvemer but still a paltry return on such a big i vestment—especially since the busines es Quaker sold to help pay for Snapple solid if unexciting performers such a pet food and beans, generated roughl $110 million in income.

Quaker's remaining food businesse can't pick up all the slack: Growth i lagging in granola bars branded oatmeal, and oth er key categories. On to of that, the powerhous Gatorade franchise, whic softened the blow fo Quaker last year, will fac greater competition thi summer, when Coca-Cola' rival Powerade revels i an Olympics sponsorship.

SURPRISE. Although slov off the mark, Quaker i trying to fight back. Uzz president of the Nortl American Beverage Div has placated distributor by scaling back some o his aggressive plans. H is also shoring up Snap ple's shaky manufacturin systems, another unpleas ant surprise uncovere only after the deal wa signed. Quaker is swal lowing a $30 millio charge to buy out onerou bottling contracts, ensur ing that Snapple plants fil orders in days instead o weeks. That's on top of a $20 million write-off fo excess inventories. This spring, Quaker will rol out new products, new packages, and a high-pro file ad campaign. Quaker CEO William D. Smithburg predicts Snapple sales will jump about 15% as the company begins "hitting on all cylinders." While the out come hinges on weather, new ads, and other unknowns, observers say Smith burg's forecast may well be on target.

It had better be. Quaker's poor performance in 1995, on top of a mediocre 1994, contributed to the October resignation of Smithburg's No. 2, President Philip A. Marineau, company sources say. If Quaker fails to rebound in 1996, it could be pushed into a breakup of its beverage and food operations. Or the rumor-prone company could be put back

Distributors thwarted Quaker's plans to meld the Snapple delivery system with Gatorade's

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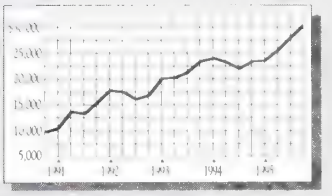

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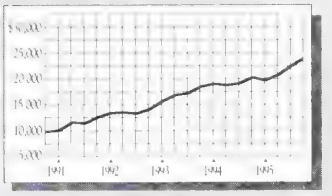

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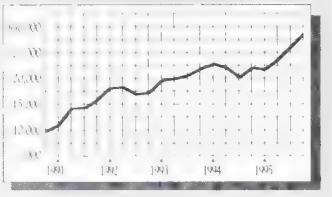

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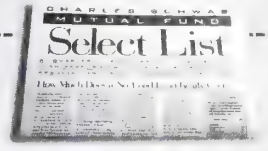

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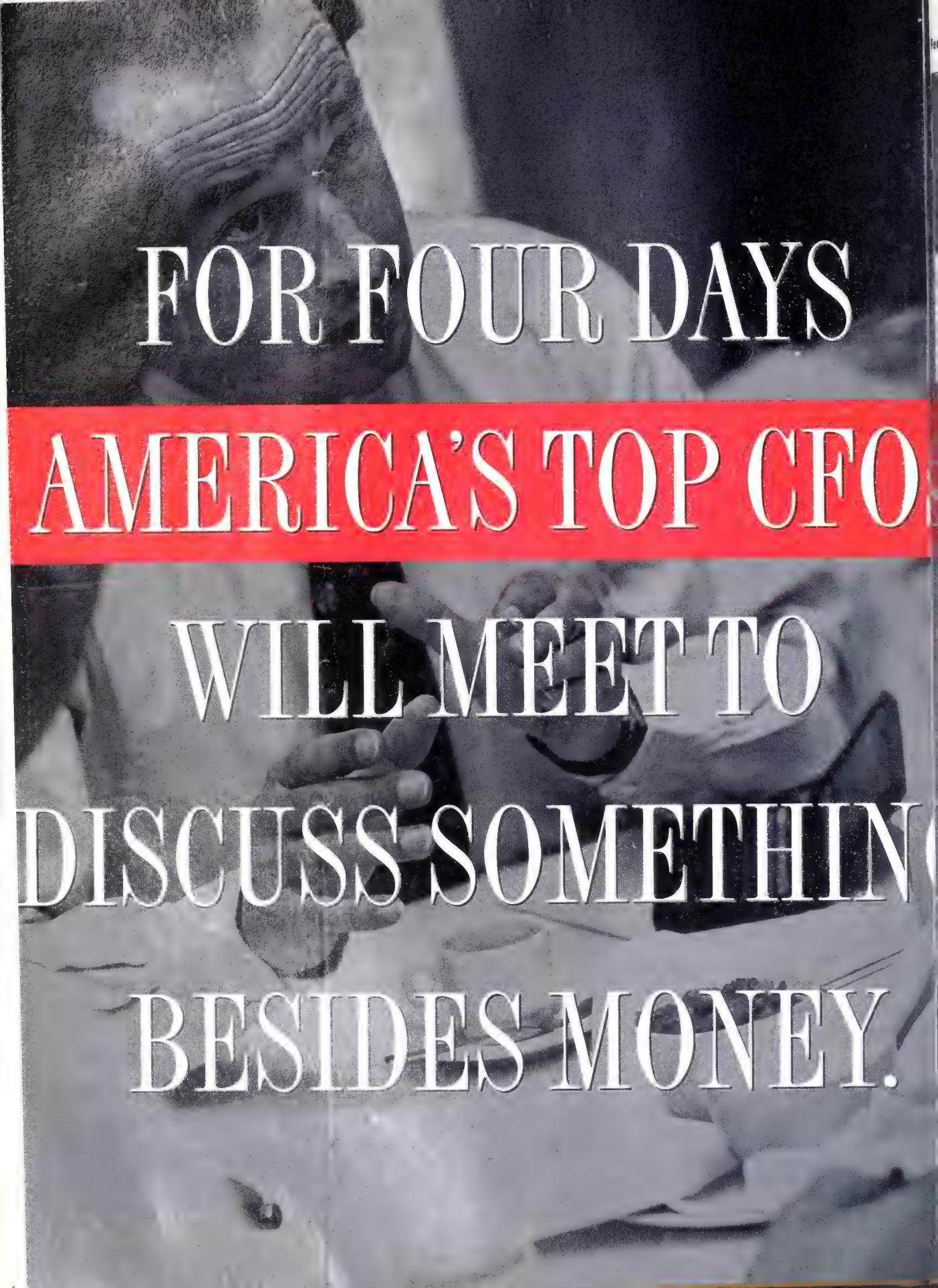
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into play as a target for acquisition, a prospect that has propped up the stock by an estimated 20%. "People think if it doesn't work out its problems, it's a takeover candidate," says analyst Arthur Cecil of T. Rowe Price Associates Inc., which owns about 1 million Quaker shares. Says Smithburg: "We are positive we can do a much better job."

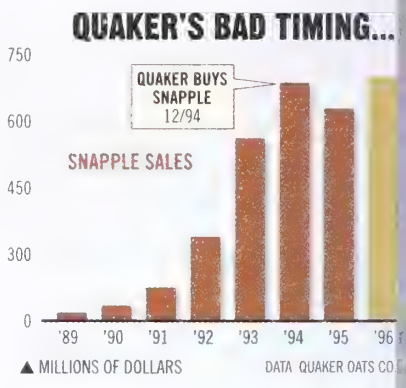
Even if Smithburg does solve the problems with operations, Snapple's long-term performance is far from assured. To pay off in years to come, Snapple must grow beyond its current Northeast and West Coast strongholds. But critics contend that Quaker overpaid for a poorly managed fad drink—just as the bubble was bursting. In fact, sales of fruit drinks and premium teas dropped 10% to 15% last year, partly because Snapple stopped driving sales. One growth segment: low-priced ready-to-drink tea, where Snapple doesn't compete.

In distribution, so critical in the beverage game, Snapple remains spotty. Distribution woes distracted Quaker during the crucial planning months before last year's summer season. Initially, Quaker wanted its efficient Gatorade warehouse-delivery system to take over Snapple's supermarket accounts from the 350 independent distributors that serviced those big chains at the time of the sale. In exchange for the chain-store routes, Snapple's distributors would be given rights to deliver Gatorade directly to mom-and-pop delis and other hard-to-service accounts where the sports drink has great potential but little presence. That partnership could have pushed both brands to new heights. But, as Uzzi concedes today, "It might have been an idea ahead of its time."

VETO POWER. Certainly, Snapple distributors, whose exclusive—and in some cases perpetual—territory contracts give them veto power, had reason to balk. For them, Snapple is much more profitable: Its $4-per-case margins are roughly double what they could make on Gatorade. And in many cases, surrendering chain-store Snapple accounts would have undermined their profits delivering other beverages to the chains. Quaker brass "just didn't know our business," says Joseph Rosamilia Sr., vice-chairman of Millrose Distributors in New Brunswick, N.J., a top Snapple dealer.

Quaker had also counted on greater manufacturing synergies. Instead, it inherited contracts that locked it into unrealistic production levels with independent bottlers the company didn't need. To avoid paying penalties and to clear up its supply-chain problems, Quaker eventually had to buy out some of those agreements. But Snapple had thrown Quaker another curve by piling up big raw-material inventories. When Quaker settled on plastic for its 32-ounce bottles and redesigned confusing labels, mountains of obsolete glass and paper had to be dumped. Quaker also had to liquidate more than 1 million cases of Snapple in outdated cans as well as some discontinued flavors and ingredients. "Snapple went very, very long in procurement," Uzzi notes wearily.

Oddly for a company built on it, Snapple fell short in marketing. By the time Quaker bought it, Snapple had been on the block for months, and a short-term mentality prevailed. Few new products were in the pipeline, and no new ads or major promos were slated for the



spring kickoff of the beverage season. Quaker revived "Wendy" ads briefly but pulled the plug in August, when they failed to drive up sales. Snapple hasn't had a campaign since. That frustrated distributors used to Snapple's guerrilla tactics. "They waited too long. Nothing was being done," gripes distributor George Julius of Beverage America Inc. in Holland, Mich.

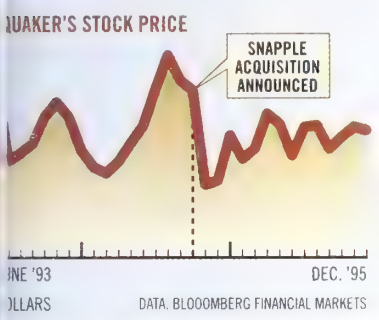
That will change when new TV spots break in April. Snapple's ad agency Kirshenbaum Bond & Partners has a tall order: The brand needs a harder sell but it must maintain its quirky image even as it becomes part of a giant corporation. The new ads ditch Wendy, who helped build Snapple's early following. Finding something that works as well

Critics contend Quaker overpaid for a fad drink–just as the bubble was bursting

ill be tough. Quaker also plans high-impact promotions, such as an under-the-bottle-cap sweepstakes. And after paring back the line by at least a dozen flavors, Quaker is rolling out new ones, including tropical-fruit Island Cocktails. reformulated diet drinks for better taste and slapped on labels that were more eye-grabbing. A new shelf-stocking scheme will reduce customer confusion by separating the tea, juice, lemonade, and diet drinks.

Of course, rivals will be on the move, too. The Pepsi-Lipton Tea Partnership will promote "real-tea taste," while Coca-Cola will keep pushing Nestea and will restage its Fruitopia juice drinks with new ads. But Eric Reinhard, general manager of the Pepsi-Lipton partnership, expects Snapple to be more of a challenge this year than during 1995. For Snapple, "there's nowhere to go but up," he says.

..LEAVES INVESTORS COLD



Some benefits of improved systems would begin to show on the bottom line this year. By cutting one-third of its independent bottlers and introducing a centralized ordering system, Quaker is curbing the production bottlenecks and out-of-stock problems that plagued the old Snapple. Streamlined plants will be able to make a range of new packages as well, including 32-ounce plastic bottles that could become a popular new size. And many observers expect Quaker to buy out weak distributors gradually, taking additional territories in-house. So far, it has cut the ranks to 200, and taken control of Florida, Texas, and Orange County, Calif.

As 1995 ended, Snapple's vital signs were stronger, with sales improving in the fall. Among brands with global ambitions, Snapple still has some of the most "colossal" prospects, says beverage consultant Tom Pirko of Bevmark Inc. For his part, Smithburg bristles at the suggestion that he bet the farm on a fad: "We certainly believe we bought a brand with legs," he insists. Now, if only it would get up off its back and run.

By Greg Burns in Chicago

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TAKEOVERS

RJR: SHAREHOLDER AT THE GATE

Bennett LeBow refines the takeover game, circa 1996

Bennett S. LeBow clearly has a bit of an image problem. His enemies have some choice—and often unprintable—epithets for him, and even a friend describes his reputation as "radioactive." No wonder: The third-tier wheeler-dealer has had two of his public companies, MAI Systems Corp. and New Valley Corp., file for bankruptcy. His current public company, Miami-based Brooke Group Ltd., operates at a loss and recently had to restructure much of its debt. And LeBow has repeatedly fended off allegations by angry Brooke shareholders that he improperly helps himself to company assets.

A minor-league bottom-fisher LeBow may have been. But as some startled folks at RJR Nabisco Inc. are learning, he may be on the verge of the big time. More and more, it looks as if he stands a reasonable chance of emerging victorious in his battle to engineer a breakup of the giant food and tobacco company. In a move some interpret as a show of confidence, LeBow on Jan. 23 moved up by almost a month the cutoff date of a shareholder resolution he is promoting that would demand that RJR spin off Nabisco immediately. The deadline for the closely watched shareholder vote is now Feb. 15.

UP FROM NOWHERE. LeBow, with his partner, raider Carl C. Icahn, controls just 4.8% of RJR's stock. When the pair began their campaign last fall by pressuring the company to spin off the remaining 80.5% of its Nabisco food business, "it seemed LeBow had no chance in hell," says Sanford C. Bernstein & Co. tobacco analyst Gary D. Black. Somewhat surprisingly, however, "people are much more receptive to LeBow's proposal than a lot of people would have thought going in," he says. "People are starting to say he does have a chance."

If he succeeds, LeBow will force the breakup of a storied company that was the focus of a titanic contest between its management and Kohlberg Kravis Roberts & Co. in the defining takeover struggle of the 1980s. But in his present campaign, LeBow may be writing some new rules for the takeover game, circa 1996. Instead of tender offers and debt financing, LeBow, armed with just 1.8% of the company's shares, is attempting to dictate the fate of RJR Nabisco by wrapping himself in the rhetoric and the tactics of the shareholder-rights movemer

LeBow figures a quick spin-off w yield an immediate 38% gain for R shareholders, who watched their shar fall from a September, 1991, high about 61 to about 28 before he beg his campaign. The stock is now at abo 34. LeBow's campaign to put a centr management issue to a shareholder vo signals "a whole new era in [shareho er] rights. This is a test of shareholde democracy," notes Salomon Brothe Inc. analyst Diana K. Temple, who al thinks a majority of shareholders w back LeBow's spin-off vote. At issue whether "shareholders have the rig to impose certain solutions or directiv on the board."

The company argues that it wants spin off Nabisco too, and has wante to for years. But it says it must wait f the tobacco-litigation environment improve. That could take until 199 says Steven F. Goldstone, a lawyer w was named RJR's chief executive in D cember. (Former CEO Charles M. Harp remains the company's chairman.)

In its appeals to shareholders to vo against the breakup proposal, RJR pain

Swashbuckler LeBow is trying to force a breakup of RJR Nabisco by borrowing the tactic of the shareholder-rights movement

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"I'LL SIGN IN BLOOD." *LeBow says he'll back off if RJR spins off Nabisco*

NO QUICK FIX: *CEO Goldstone opposes a fast spin-off*

LeBow as an irresponsible quick-buck artist who is only now pushing the spin-off because RJR in May turned down a deal he proposed to Harper and Goldstone. LeBow's proposal then was for RJR to be acquired by Brooke's Liggett tobacco subsidiary. LeBow's board would then have spun off Nabisco. LeBow's board, and not RJR's, was to assume the legal risk if tobacco plaintiffs or RJR bondholders sued. The payoff for LeBow: a 20% stake in the merged Liggett-RJR. His partner in the deal, German tobacco company Reemtsma Cigarettenfabriken, would have formed a joint venture with RJR's international operations.

NOW, "VOYAGEUR." Harper says LeBow was "turned down right there, to his face." But LeBow maintains that the deal was taken seriously enough by RJR for Goldstone to meet with LeBow's lawyers three more times that summer. When all hopes of a friendly deal involving Liggett died in July, LeBow already owned 723,000 RJR shares. He was convinced that a great deal of money could still be made if RJR were to overcome its litigation concerns and spin off Nabisco immediately. LeBow thinks RJR won't spin off Nabisco because its directors fear potential personal liability under a legal concept called "fraudulent conveyance," which may arise if a company improperly shuffles assets. Goldstone says personal liability is not a major concern of the board. LeBow teamed up with major Brooke debt holder Icahn, who bought 8 million shares but leaves the heavy lifting to LeBow.

The affable Harper grows almost apoplectic when discussing LeBow. He dismisses Liggett as "a little rinky-dink company" and LeBow as a "voyageur hopping out of his canoe on the shore of the Hudson." If LeBow isn't exactly the itinerant fur trader Harper paints him as, the mantle of shareholder advocate nevertheless seems to rest a bit awkwardly on his shoulders. As RJR hastens to point out, his holdings have been marked by bankruptcies, insider deals, and shareholder lawsuits. LeBow, 58, counters that he invests in troubled companies, that his personal loans from Brooke have been repaid with interest, and that investors who stayed with Brooke from 1991 through 1995 have reaped a compound annual rate of return of 26.8%, compared with a 3.8% return for RJR since its 1991 initial public offering. But his reputation is a side issue, LeBow says. "What else do they have to talk about? Why don't they talk about the issues?"

Goldstone argues that the real issue is RJR Nabisco's continuing viability as a company. LeBow's spin-off proposal "would have a terribly destabilizing impact," says attorney Martin Lipton, who represents RJR in the consent solicitation. If the resolution passes, "it would make it extremely difficult to manage the company. People would have real questions as to the future course of the business and what is going to happen."

Maybe that's why RJR Nabisco seems willing to cede the high ground of shareholder democracy to LeBow. Goldstone vows that management and the board will not comply with calls for a quick spin-off, even if shareholders overwhelmingly back the plan. "If LeBow were to convince a majority of our shareholders to support [the immediate spin-off] resolution, the board would continue to do just what it's doing," Goldstone says.

LeBow seizes on such imperiousness with the populist gusto of an old-time pol. "This is a new high in contempt for shareholder rights. Now is the time to speak—or forever hold your... stock," LeBow proclaimed in full-page ads in *The New York Times* on Jan. 22 and *The Wall Street Journal* on Jan. 23, which bore the headline "R to Shareholders: DR DEAD!" To assert contr over their compan shareholders we urged to send in co sent solicitation car supporting the spin-o LeBow's ad even list a site on the Wor Wide Web that provid more information.

Several big shar holders tell BUSINE WEEK they plan to ba LeBow. "Although we haven't met wi RJR yet, we currently lean toward vo ing for the spin-off," says Jeffrey Altman of Michael Price's Mutual S ries Fund. Goldstone says he is "ve confident" that LeBow won't have t votes he needs in the end.

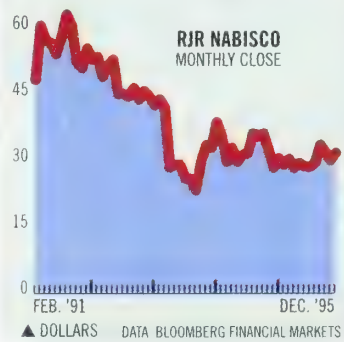
CALLING RJR'S BLUFF. But by movi up the cutoff date for the vote, LeBo is indicating that he believes he c muster the votes he needs by Feb. LeBow says he hopes that RJR reco siders its position and obeys its shar holders' wishes. "I could be the wo guy in the world, [but] if they'd ju spin off Nabisco to the shareholde I'll sign in blood that we've done wh we want, and we'll go off."

But he knows RJR says that it wo budge, and he's planning to call bluff. Though LeBow claims that does not want to actually control RJ board of directors or manage the co pany, he and Icahn have submitted alternate slate of directors for RJ annual meeting in April. His decision move up the spin-off vote may be sign that he intends to try to gain co trol of the board.

If he wins the vote a month earl than anticipated—and RJR ignor the mandate—LeBo will have more tim before the annu meeting to file proxy and campai for shareholders t vote for his alterna slate of directors. A self-respecting cha pion of shareholde rights would hav any alternative.

By Elizabeth Le in New York an Gail DeGeorge Miami

JOE CAMEL'S BLUES



How Should You Invest Your IRA? (You Decide.)

The Right Place At The Right Time?

The Right Place *Over* Time?

TWENTIETH CENTURY'S GROWTH EQUITY FUNDS

Average Annual Total Returns *as of 12/31/95*[2]

	1-Year	5-Year	10-Year	Life of Fund
GROWTH *Investors*	20.4%	14.8%	14.2%	18.2% (6/30/71)
ULTRA *Investors*	37.7%	25.0%	19.8%	17.8% (11/2/81)
VISTA *Investors*	46.1%	22.4%	17.1%	14.3% (11/25/80)
SELECT *Investors*	22.7%	10.2%	11.8%	16.5% (6/30/71)
HERITAGE *Investors*	26.7%	16.5%	—	16.0% (11/10/87)

Past performance is no guarantee of future results

Chasing the hottest mutual funds might be exciting—for a while. But we think it's better to focus on funds that have already established a strong, long-term record. While the past doesn't guarantee the future, we believe Twentieth Century's growth funds have a record that speaks for itself. Call us toll free and ask about our **no-fee**[1]**, no-load IRA: 1-800-345-2021**. We'll send a prospectus with more details, including all charges, expenses and minimums. Please read it carefully before you invest. Let Twentieth Century help you make the most of your strongest allies: time and patience.

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A GOOD CHOICE FOR YOUR IRA, 401(k), OR SEP/SARSEP

STRATEGIES

IS MOTOROLA A BIT TOO PATIENT?

While it waits for long-term bets to pay off, profits erode

For on-the-go cellular phone users, few things are more annoying than losing a connection in the middle of a call. But for global market leader Motorola Inc., lost calls are more than an annoyance: AirTouch Communications Inc. was supposed to have a sophisticated multimillion dollar digital-cellular system from Motorola up and running in Los Angeles by early 1995. But with technical problems still causing lines to go dead, AirTouch won't put customers on the system—or finish paying Motorola—until the kinks are cleared up. "We are being finicky," says spokeswoman Amy Damianakes. "We want it to be as good as the existing analog service or better."

That hardly seems like a lot to ask of Motorola, the world's biggest maker of cell phones and pagers. After all, as the global leader in two of the world's fastest-growing technologies—wireless communications and semiconductors—Motorola has long been lauded as one of America's technology giants. But as the Schaumburg (Ill.)-based company struggles to regain momentum in the tough U.S. cellular market, it is facing a host of uncomfortable new questions. The biggest: Has Motorola hit a bit of momentary turbulence, or is the high-flying star finally coming down to earth?

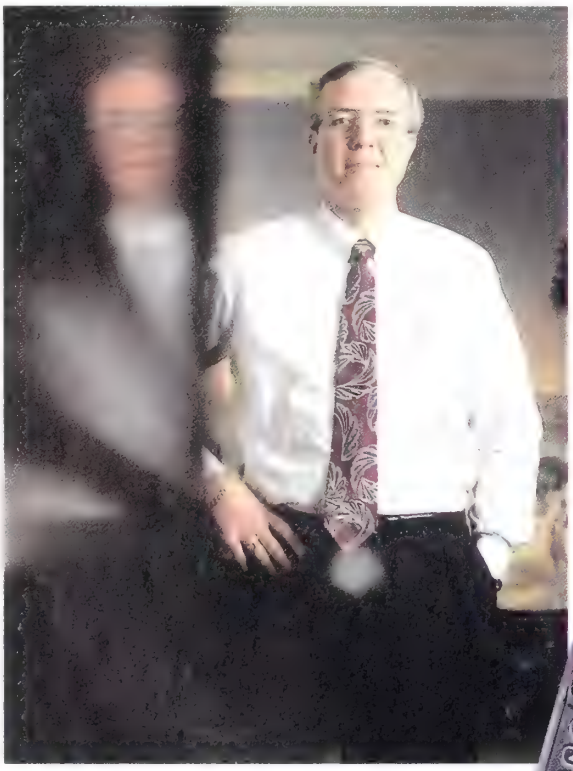
The queries picked up force early in January, after the company announced that fourth-quarter earnings would fall 16%, to $432 million. Company officials blamed much of the slide on cellular, yet difficulties there aren't all that Motorola has to worry about these days. CEO Gary L. Tooker, 56, and President Christopher B. Galvin, 45, who together make up the office of chief executive, are set on keeping Motorola in a broad array of markets: Its products range from tiny chips that go into cars to U.S. Army ground stations for airborne surveillance equipment. But with competition rising and problems cropping up on several fronts, investors are starting to ask if Motorola has its fingers in too many pies.

Other high-profile Motorola products—such as the PowerPC chip and the Envoy personal digital assistant—have bee slow to catch on. Iridium Inc.'s cost global satellite-phone system, for whic Motorola is the prime contractor, h had trouble finding financial backers. A perhaps most worrying is a naggi question that has trailed the compa for several years: With an increasi share of its products going into consum markets, can the engineers who run M torola learn to do a better job of ma keting their wares? "They're spread r ally thin," warns Susan Kalla, an analy with Stamford (Conn.)-based SoundVie Financial Group.

With all that to worry about, it's surprise that Wall Street has thrown a red flag. After soaring from 11 in 19 to 82 last September, Motorola shar have fallen about 36%, to around 53. F the full year, Motorola managed to boo profits 14%, to $1.78 billion, on a sal gain of 22%, to $27 billion. But with t company warning that earnings compa isons will remain "difficult" this ye analysts surveyed by First Call expe 1996 profits to rise just 2%.

NO RETREAT. Not that Motorola is in di straits by any means. But until recent this was a company that seemed infal ble. As it moved from strength strength in its core technology market revenues have mo than doubled sin 1989, while incon jumped 39% annual But even insiders s that pace can't be mai tained. "It can't go forever," says on "Maybe 15% a year is r alistic, but [growth isn't g ing to continue] at 30%."

For all the storm, c Tooker sees no need for r trenchment. A plain-speaki electrical engineer who join the company in 1962, he's w respect as a no-nonsense op ating manager who honed h skills in the cutthroat semicondu tor business. He says he has no i tention of pulling back on the lon term strategy by which Motorola bu its name. The style was set by form Chairman Robert W. Galvin—Christ pher's father, who remains chairman the board's executive committee—a continued under charismatic CEO Geor M. C. Fisher: placing farsighted bets or wide array of technologies. Tooker, w took the top job when Fisher went Eastman Kodak Co. in 1993, argues th Motorola must stick to that strate while expanding in fast-growing dev oping markets. "Our opportunities ha



ON HOLD

Gary Tooker is counting on new digital technology to revive cellular sales, but analog phones still dominate the U.S. market

robably never been better," he ys.

Lately, though, Motorola has emed to have unwonted diffi- ulty in making the most of its portunities. The biggest chal- nge remains in cellular, which ovides 40% of sales. There, otorola's problems are vofold. After a three-year urt in which growth pped 30% a year, de- and in the U.S. is slow- g. At the same time, candinavian rivals such as .M. Ericsson and Nokia e stepping up efforts in e U.S. The result: a vicious ice war that has hit Motoro- 's earnings particularly hard.

Motorola's market share is so slipping. From 42% of the .S. market in 1994, Sound- ew analyst Kalla expects Mo- rola's share to fall to 37% this ar; Nokia meanwhile will go om 21% to 32%. Motorola at- ibutes the drop largely to ex- ssive orders in late 1994 that oated inventories, but rivals crow that ey're gaining. "We've been winning are for three years," says Anders rstensson, executive vice-president of icsson's U.S. arm. And look out: While panese manufacturers such as Sony, nasonic, and Toshiba have largely lost t so far, they intend to return with a ngeance in the market for low-cost rsonal communications services (PCS) ones next year.

Nor are the cellular problems limited the U.S.; in Europe, too, Motorola's ce has fallen from 38% in 1994 to a ojected 33% in 1996. In part, that's e to an aggressive push by Nokia and icsson to grab share as a more so- isticated digital cellular service known GSM takes hold there.

And that points to further questions r Motorola as the U.S. begins to shift digital cellular. Motorola is placing big ts on a newer technology known as MA—code division multiple access. Cel- lar service providers like CDMA because offers far higher call-carrying capacity an GSM. But the technology still has me bugs, as the Los Angeles experi- ice shows. Analysts say substantial MA sales may not begin until late 1997, d some competitors remain skeptical. Ve don't consider it to be economically able in its present state on a large ale," says Per Bengtson, a spokesman r Ericsson. With CDMA likely to take ne, the company is emphasizing GSM.

Still, Tooker says Motorola plans to nker down: He expects cellular will e a strong rebound when PCS phones the markets—probably by 1997—and

AS MOTOROLA FACES TOUGH CHALLENGES...

CELLULAR PHONES Increased competition and slowing demand have cut Motorola's market share and slashed earnings. Sales of improved digital phones have been slow to take off.

POWERPC CHIP This microprocessor was supposed to edge out Intel's Pentium, but troubles at co-developer Apple Computer cloud its prospects.

MARKETING As cell phones and other products hit mass markets, Motorola's engineers will come up against marketing powerhouses such as Sony and Panasonic.

ENVOY PDA Priced at $1,000 to $1,500, Motorola's wireless personal digital assistant has sold poorly. Now, Motorola is focusing more on business customers.

ENVOY PDA

spur demand again. But problems may not be so readily solved for the PowerPC, the $1 billion chip developed by Motorola in partnership with Apple Computer Inc. and IBM. Introduced with fanfare in 1993 with Apple as its flagship customer, the PowerPC was supposed to become a major rival to Intel Corp.'s Pentium. But although Motorola is now getting lots of PowerPC orders from makers of settop boxes, server computers, and other special machines, the chip hasn't created anything like the breakthrough expected.

Apple's struggles have hardly helped: Its sliding market share has meant fewer chip sales than expected. Without Apple as a base, few other PC makers have adopted the chip. Although Motorola continues to pour money into software development and is creating its own PowerPC-based computer systems in hopes of jump-starting the market, outsiders think its chances are slim.

Iridium, the $3.4 billion satellite phone system of which Motorola is the main backer, is also running into outside skepticism. The ring of satellites should allow callers to use wireless phones anywhere around the world to call anywhere, but several rivals are vying for the risky market. Although Tooker predicts that Iridium will eventually be a big success—the first of 66 satellites are due to be launched late this year—few outsiders are ready to back it. Iridium has raised only $1.6 billion so far and last fall had to scrap a $300 million junk-bond offering in the face of investor disinterest.

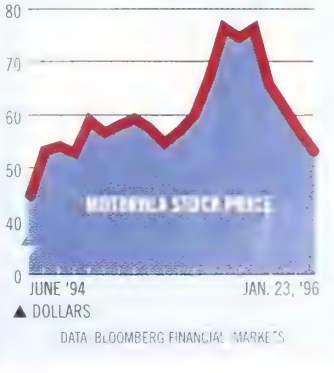
OUTSIDE HELP. Despite the crop of difficulties, Tooker denies that the company is spread too thin. One thing he and Galvin will need to concentrate on is better marketing. With an ever-increasing share of their products going to consumer markets, Motorola execs have said for years that they need to boost their consumer marketing know-how. But the engineering-led company has been slow to change. A case in point: The Envoy PDA was technically strong but priced far too high for the market at $1,000 to $1,500.

To improve its marketing savvy, the board asked Procter & Gamble Co. Chairman and CEO John E. Pepper to become a director last year. Although "selling a cellular phone isn't the same as selling soap," Pepper should help Motorola figure out how to "market consumer products in a way that it may not have considered," says Director B. Kenneth West, the former chairman of Harris Bankcorp Inc. Motorola has also beefed up marketing by bringing in executives from the likes of Black & Decker Corp. and Mattel Inc.

But elsewhere, Tooker says few changes are planned despite the earnings slide. "This is a few days in the life of a company that's decades old," he says. "We think we're making balanced investments for the future." Nor does the board appear worried. "There may be some unruliness in the competitive environment, but it's worth hanging in," says director West. Both argue that by mid-1997—when they expect cellular to revive, the PowerPC and a relaunched Envoy to take off, and the bet on CDMA to pay off—a fresh surge in profits and revenues will mute the short-term skeptics. Though questions are growing, given Motorola's record, few are willing to count it out yet.

By Peter Coy in New York, with Ron Stodghill II in Chicago

...INVESTORS GET WORRIED



EDITED BY AMY DUNKIN

NOT ALL TAX SOFTWARE IS CREATED EQUAL

Last year, the makers of tax software programs taxed the loyalty of their customers. A spate of software bugs that created calculation errors or missed deductions, coupled with perpetually jammed phone help lines, left many users of leading programs such as TurboTax and Kiplinger TaxCut wondering if the benefits outweigh the hassles.

Should you trust your taxes to a software program? For many individuals, the answer is still yes. Despite its flaws, income-tax software remains a better alternative to using a pencil, calculator, and scratch pad—which can add hours to your work and increase the chances of a math error. And for their part, the makers of the leading programs vow they have taken steps to minimize the risk of last year's problems recurring.

DISCLOSURE. Instead of ripping up their programs to build in more features, most of the companies are concentrating on making sure their programs work right. Intuit also says it has doubled the size of its technical-support staff, to 500, to field questions about TurboTax and MacInTax. And all the software publishers pledge they'll be more diligent in reporting bugs. In years past, they tended to wait until late in tax season to issue an all-inclusive list. But after last year's fiascoes, they have vowed to get the word out sooner: Intuit and Parsons through their Internet Web sites and others through on- [illegible], fax, and phone.

Given the relative lack of new features to compare and [illegible]

cided to subject this year's crop of tax programs to a practical test: a hypothetical tax return that was so complex it bordered on the diabolical. This return from Hell was the handiwork of Alfred C. Giovetti, a Catonsville (Md.) certified public accountant and accounting instructor whose students include Internal Revenue Service agents. Giovetti created a tax return for a fiftysomething couple earning a combined $200,000 from a variety of sources including salaries, employee stock options, and rental property. He tested five popular programs—TurboTax, Kiplinger TaxCut, Simply Tax, Personal Tax Edge, and Perfect Tax—then stacked up their results against a $3,500 program popular among professional tax practitioners.

His finding? While all of the programs—with the notable exception of Perfect Tax—interpreted the tax code accurately, they nonetheless pose many critical questions so ambiguously that any user lacking a CPA license could answer some inaccurately—and risk incurring not just penalties but an IRS audit. "These programs lull you into a sense of false security," says Giovetti. "We assume the computer knows more than it often does."

TROUBLE SPOT. Particularly troubling was how most programs breezily ask users up front whether they think they are a candidate for the alternative minimum tax, which some people must pay if they have a large number of deductions. Answer "no," and chances are the software won't determine afterward, based on your subsequent in-

ies, whether your initial dgment was right. When ovetti added a generous llop of deductions and exptions into his formula—nich would have subjected s make-believe couple to e AMT—the programs unrestimated the correct tax .bility by as much as 0,000. The moral: For highcome households with exnsive deductions, exempons, and other shelters, tax ftware is no alternative to good accountant.

For the rest of us, the st program might be Taxit, which allows you to mplete your return using interview format that's ore intuitive and logically ranged than those of rivals. xCut's "audit" feature—nich flags answers that uld trigger a visit from the s—is so thorough it catches screpancies that only a CPA ight be expected to find. nd in Giovetti's test, only xCut detected that a prior nployer made a premature tirement payout without thholding the mandatory %—a move that, if not ught, can subject the reoient to an IRS penalty.

T WORTH. Not that Taxit is without flaws. Like her programs, it doesn't alays automatically transfer nswers to other relevant ctions of the return: Users, r instance, must manually rry the gain from Form 84—which handles casual- losses—to Schedule D. nd while the program's au- t feature will take you to e point in our return here a problem may lie, it then returns ou to the beginning of the udit function.

Giving TaxCut a run for s money is Personal Tax dge. Don't be fooled by its 9 price tag—Tax Edge's interview and audit features e as strong as any of its gher-priced rivals. Admitdly, Tax Edge lacks the exnsive help features of Taxit and TurboTax. But the deluxe CD-ROM version of Tax Edge, which was acquired two years ago by Intuit, also comes with access to the company's Web site—which provides extensive online help. Another bonus: Tax Edge includes a set of nifty investment calculators that can be used long after tax season and are worth the $19 price by themselves.

Tax Edge fared well in Giovetti's test: The program takes more care than others to prevent users from taking the same deduction twice by alerting you when an entry has been transferred to another form—although, irritatingly, it won't always handle the transfer automatically. Tax Edge will also appeal to last year's users of Novell's Tax Saver, which was discontinued, because both programs share the same underlying computer code.

Mildly disappointing was the performance of TurboTax, which despite being the best-selling tax program, still hasn't worked out some annoying kinks in its interface. Don't skip around various sections of the interview process, or between the interview and the underlying tax forms, because TurboTax won't always take you back to the question you answered last—forcing you to waste a lot of time relocating your place.

Giovetti also found that TurboTax isn't always good at remembering how you responded to relevant questions earlier in the Q&A, either. When you answer questions about Form 1099-R, for instance, it advises you that you'll also have to complete the related Form 5329—but doesn't provide a similar reminder later on, when you actually need it. To its credit, TurboTax reviews each form as you complete it—rather than just when you finish the whole process—giving you a chance to correct inconsistencies while the information is fresh in your mind and you have the documentation at your fingertips.

TWO DOGS. Then there's Simply Tax, which is, well, simply awful. At first, it appears that Computer Associates International finally got it right with the three-year-old program. The interview function begins impressively, with entries transferred automatically to other relevant portions of the return. But you quickly get the impression that the designers of Simply Tax ran out of time because the Q&A function abruptly becomes less intuitive and simply starts throwing forms at the user to fill in. Even then, some of the forms are displayed in a small typeface that's almost illegible on a 15-inch monitor. What's more, Simply Tax's handling of depreciation is too simplistic—not allowing you to choose the number of years or the method.

Simply Tax only looks good when compared with Perfect Tax, a $79 program available by direct mail from Dallas-based Financial Services Marketing. Perfect Tax's poor performance is baffling, given that its parent also sells more expensive versions to professional tax practitioners. But in Giovetti's hypothetical return, Perfect Tax miscalculated the child-care credit by a hefty $480 and didn't provide the proper deduction for margin-interest expense or for rental property. Against this program, a pencil, pad, and calculator almost seem preferable. *Dean Foust*

YOUR TAXES

Tax Advice in a Box

PROGRAM/COST* MAKER/PHONE	FORMAT	SYSTEM REQUIREMENTS**	COMMENTS
TURBOTAX $40 Intuit 800 964-1040	Win, Win95, DOS, Macintosh, CD-ROM	4 MB RAM, 20 MB HD	Includes Web browser that connects directly to Intuit's Internet site for late-breaking bug reports, tax code changes. Number of states: 45.
KIPLINGER TAXCUT $20 Meca Software 800 235-4060	Windows 3.1 Macintosh, CD-ROM	4 MB RAM 10 MB HD	Easiest Q&A interview and strong audit capabilities. Number of states: 23 Win, 2 Macintosh.
PERSONAL TAX EDGE $19 Intuit 800 223-6925	Windows, DOS, Macintosh, CD-ROM	2 MB RAM 13 MB HD	Powerful investment calculators; enhanced tax help drawn from popular J.K. Lasser guide. Number of states: 43.
SIMPLY TAX $20 Computer Associates 800 773-5445	Win, Win95, CD-ROM	8 MB RAM 13 MB HD	Simply awful. Interview feature is weak; forms illegible. Number of states: 20.
PERFECT TAX $79 Financial Services Marketing 800 525-5611	DOS	640K RAM 3.5 MB HD	Pricey DOS program. Miscalculated child-care credit, margin-interest expense, and rental income. No state editions.

* Street price for federal editions on diskette; CD-ROM versions higher. State programs cost $18 to $25 each.
** Requirements for Windows 3.1. May differ for other operating systems. RAM is random access memory, HD is hard-drive space

DATA BUSINESS WEEK

REMEMBER THOSE '95 GAINS? SO DOES THE IRS

In 1995, the markets made you richer. Your mutual funds zoomed, and you sold stocks and bonds at huge gains. Now, brace yourself for tax season.

Since Congress didn't get around to passing the capital-gains tax cut that its leaders promised, you owe 28% on the difference between your selling price and your cost basis on all transactions. Plus you owe 28% on all mutual-fund capital-gains distributions. All those gains could make the income reported on the W-2 from your job look downright skimpy.

If these profits were a big chunk of your total income in 1995, you should have been making estimated tax payments on a quarterly basis. If you paid in at least 90% of your actual 1995 tax due by Jan. 16, 1996, or you paid in 100% of your 1994 tax due—110% if your 1994 adjusted gross income (AGI) was more than $150,000—then Apr. 15 should not be so stressful. But if you haven't protected yourself, there's nothing you can do now except figure your interest (9% per annum) and penalties (.5% a month) and pay those in addition to your tax.

HELP WITH HISTORY. Even if you have been estimating your taxes quarterly, you may not have made exact computations. As a result, you may still have a big data collection job ahead of you. If you sold any mutual-fund shares or switched within fund families, then you have to determine the cost basis of the shares you sold. An increasing number of mutual-fund companies are providing cost data on their yearend statements. But if you have owned the fund for a long time, you may have to call the fund company to get cost records going back many years. Allow four to six weeks for delivery.

It's simpler to obtain cost data for individual stocks and bonds. Your broker should be able to supply that information if the firm is truly full-service. If not, call the issuing company's investor-relations department to obtain the price histories. Be sure to take stock splits into account: A stock currently selling at $100 may appear to have a cost basis of $30 in 1990. But if the stock split 2-for-1 in 1992, then its adjusted basis is really $15.

If you have sold only part of your position in a stock or a mutual fund, then you've got a bit more work to do. Let's say you sold 25 shares of XYZ Corp. stock in 1995 for $10 per share. You bought 25 shares in 1991 for $2, 25 in 1992 for $4, 25 in 1993 for $6, and 25 in 1994 for $8. Which shares did you sell? You're allowed to choose—and typically you would pick the $8 shares, since they would yield the lowest capital gain.

In contrast, if these were shares in a mutual fund, you could only use the "specific identification" method if you had notified your fund company at the time of the transaction which shares you wished to sell. Otherwise, you would either use the first-in, first-out method or take an average cost. The FIFO method assumes that the shares you sold in 1995 came from your earliest purchase way back when. Average cost is the total number of shares you own divided into your total dollars invested, regardless of the timing of the purchase.

Your mutual fund's yearend statement, the 1099-B, will summarize all of your purchases and sales for the year. Your mutual fund will also issue you a 1099-DIV which tells you how much you earned in ordinary dividends and capital gains. The capital-gains distribution is the gain that the mutual fund's portfolio manager realized from stock and bond transactions.

NEW STANDARD. After you get done reporting all your income, see how much you can offset with expenses. Here, the pickings are slim. Your medical expenses must exceed 7.5% of your adjusted gross income before you get any tax benefit. That means you need to have paid out of pocket more than $7,500 in medical bills on $100,000 of AGI. You can deduct state income taxes, home mortgage interest and home-equity-line interest but not credit-card debt. Your charitable contributions over $250 must be accompanied by a receipt from the charity that says you didn't receive anything of value. (Be more writing off the painting that you bought at a charity auction.) Finally, there's a catch-all category, miscellaneous itemized deductions that includes unreimbursed employee expenses and tax-prep fees. These must exceed 2% of your AGI to count.

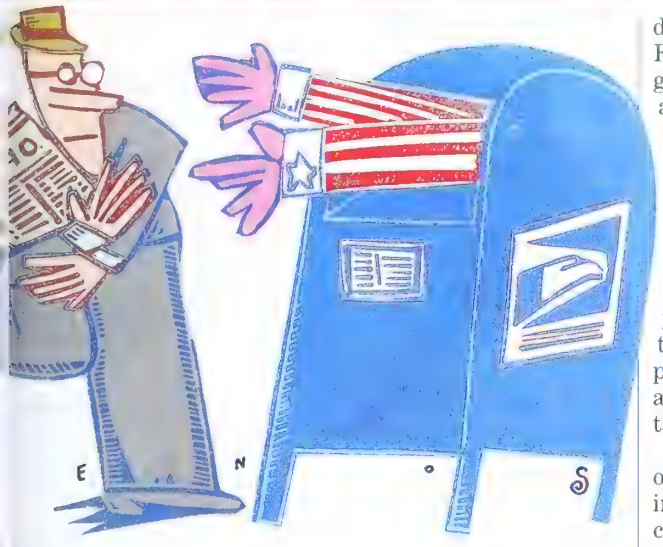
Don't forget exemptions for you, your spouse, and your dependents. Exemptions reduce your income by $2,[illegible] per person. This year, you have a new standard to meet. "You're required to have a Social Security number for the dependents you claim on your return," says Mark Down, a partner with Coopers & Lybrand in St. Louis. "That rule came into effect because people were claiming individuals who weren't dependents—even living things that weren't individuals." *Stuart Weis*

Expenses You Can't Deduct

- Adoptions
- Funerals
- Commuting
- Health spas
- Parking tickets
- Life insurance premiums
- Meals while working late
- Marriage licenses
- Home repairs
- Personal legal bills
- Residential telephone

DATA ERNST & YOUNG

YOUR TAXES



HIS MAY BE THE YEAR O THINK EXTENSION

'omises, promises. u liquidated a big unk of your portfo- in 1995 because ir congressman promised re would be a capital- ins tax cut roactive to Jan. 995. Here it is February, 6, and there's still no bud- deal.

f you're still hoping to get ax break for 1995, should put aside your tax re- n until there's an agree- nt in Washington and per- s file an extension beyond r. 15? After all, the cur- t version of the congres- nal tax proposal still mises that a capital-gains cut will be retroactive to . 1, 1995. Or should you now and then amend your urn if and when the law nges?

f you file now, you will according to the current —28% on capital gains. If law is changed retroac- ly, you would file a Form 0X to amend it, refigur- your tax under the new s. You can either request efund check or apply the savings to your 1996 tax r. Actually, you have three years from the date of your original return to file an amended tax return.

Typically, the only advantage to filing sooner rather than later is if the government owes you money. True, it's nice to get that dreaded task over and done with, so you don't drag out the tax season until Labor Day. You would be filing an amended return if and only if Congress comes through with a retroactive change. The big drawback is that you must pay a higher amount of tax up front based on the current law. And if you're paying for an accountant's time, filing and amending is more time-consuming and costly than extending.

BUYING TIME. In contrast, filing an extension is a snap. Using a postcard-size 4868 form, you can get an automatic extension of up to four months. A second extension can be obtained for another two months, until Oct. 15, if need be. But be warned: Filing an extension does not mean dragging out the time before paying Uncle Sam. Instead of figuring your tax to the penny, you are allowed to simply estimate your tax due and pay it with your Form 4868. Of course, if Congress doesn't come through as you had hoped, then your estimated payment had better be close to your actual tax due. If your estimate is at least 90%, you will pay an interest charge figured at an annual rate of 9% on the balance due. If your estimate is too low, tack on an additional 0.5% per month penalty. Interest and penalty charges are not tax deductible.

Even if you're not planning on a capital-gains tax cut, filing an extension has its charms. For one thing, it gives you more time to get your tax records together. This can be important if you have lots of capital-gains transactions requiring you to hunt for the cost basis of the securities. If you have redeemed mutual-fund shares during 1995, it can take a long time to collect cost records, particularly if you have owned the fund for many years.

In addition, many investors in limited partnerships do not receive their K-1 forms, which report 1995 earnings, until late March. Self-employed people can use an extension to give them extra time to fund a retirement plan. You have until the date you actually file to make your 1995 contribution. Finally, if you're the type who needs a lot of hand-holding from your accountant, you're more likely to get it in the summer than during the busy season.

Last year, President Clinton waited until the first week in April to sign a law that extended health-insurance deductions for self-employed individuals. The law was retroactive to 1994, which means that anyone who filed a return prior to Clinton's action would have had to file an amended return in order to receive the deduction. For many taxpayers, the extra accounting fees were not worth the additional tax benefit.

DON'T OVERPAY. This year, another law that's up in the air is whether tuition reimbursement from employers is still excludable from income. Because that provision has not yet officially been extended, the W-2 from your employer will reflect those reimbursements. But if you received a tuition reimbursement last year, you might want to request an extension so you don't overpay now and then have to amend your return later.

All of this uncertainty has many accountants, as well as their clients, in a tizzy. "We've got loaded up on our computer system all the tax forms and calculations as the law stands now," says James Vonachen, a tax partner with Clifton, Gunderson & Co. in Denver. "How in the world are people supposed to do their tax returns when the forms might not reflect the law?" The simple answer: When in doubt, file an extension and let things sort themselves out. *Stuart Weiss*

YOUR TAXES

WORTH NOTING

- **PAY-UP TIME.** When President Clinton raised taxes on upper-income individuals two years ago, he softened the blow by allowing the extra 1993 tax to be paid on the installment plan—interest-free. The final payment is due this Apr. 15. Just in case anyone forgets, the IRS will send out a reminder notice in March.
- **H IS FOR HELP.** If you employ domestic help, you'll probably have a new form to fill out this year: Schedule H. You must compute Social Security, Medicare, and income taxes for any baby-sitter, gardener, or other household worker who received at least $1,000 in wages in 1995. Schedule H puts you in compliance with the "nanny tax" law Clinton signed in October, 1994.

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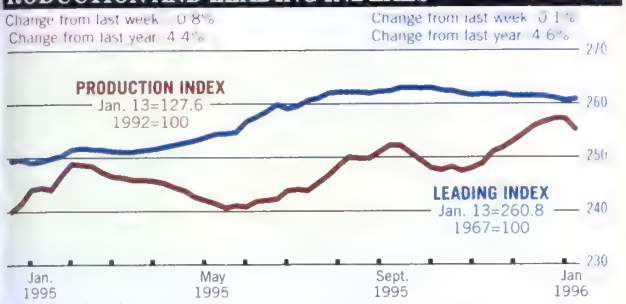
Business Week Index

PRODUCTION AND LEADING INDEXES



Indexes are 4-week moving averages

The production index fell during the week ended Jan. 13. Before calculation of the four-week moving average, the index dropped to just 125.7, from 128.3. The East Coast blizzard caused steep cuts in auto, truck, and coal output as well as a drop in rail-freight traffic.

The leading index edged up slightly in the latest week. The unaveraged index increased to 262.7, from 261. Faster growth in M2 and real estate loans offset lower stock prices and a bigger decline in materials prices.

The production index copyright 1996 by The McGraw-Hill Companies BW leading index copyright 1996 by CIBCR

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (1/20) thous. of net tons	2,035	2,031#	1.9
AUTOS (1/20) units	102,985	96,550r#	-9.1
TRUCKS (1/20) units	98,109	95,653r#	7.8
ELECTRIC POWER (1/20) millions of kilowatt-hrs.	62,943	67,271#	6.3
CRUDE-OIL REFINING (1/20) thous. of bbl./day	13,772	13,597#	1.6
COAL (1/13) thous. of net tons	17,149#	17,721	-18.6
PAPERBOARD (1/13) thous. of tons	NA#	NA	NA
PAPER (1/13) thous. of tons	NA#	NA	NA
LUMBER (1/13) millions of ft.	458.4#	313.1	-1.3
RAIL FREIGHT (1/13) billions of ton-miles	22.2#	21.1	-8.3

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA[1], SFPA[2], Association of American Railroads

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (1/19) S&P 500	606.94	606.18	29.6
CORPORATE BOND YIELD, Aaa (1/19)	6.80%	6.86%	-19.4
INDUSTRIAL MATERIALS PRICES (1/19)	110.2	111.0	-4.1
BUSINESS FAILURES (1/12)	NA	NA	NA
REAL ESTATE LOANS (1/10) billions	$508.0	$503.7r	9.9
MONEY SUPPLY, M2 (1/8) billions	$3,755.8	$3,749.6r	4.7
INITIAL CLAIMS, UNEMPLOYMENT (1/6) thous.	394	372	10.7

Sources: Center for International Business Cycle Research (CIBCR), Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/24) $/troy oz.	402.500	397.700	5.3
STEEL SCRAP (1/23) #1 heavy, $/ton	144.50	144.50	-1.3
COPPER (1/20) ¢/lb.	118.5	121.3	-18.6
ALUMINUM (1/20) ¢/lb.	75.5	77.0	-24.9
COTTON (1/20) strict low middling 1-1/16 in., ¢/lb.	80.28	81.16	-9.2
OIL (1/23) $/bbl.	18.74	18.14	0.4

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (1/23)	5.44%	5.84%	5.42%
COMMERCIAL PAPER (1/24) 3-month	5.35	5.41	6.24
CERTIFICATES OF DEPOSIT (1/24) 3-month	5.36	5.39	6.22
FIXED MORTGAGE (1/19) 30-year	7.30	7.37	9.25
ADJUSTABLE MORTGAGE (1/19) one-year	5.59	5.50	6.90
PRIME (1/24)	8.50	8.50	8.50

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/24)	106.81	105.42	99.47
GERMAN MARK (1/24)	1.48	1.46	1.51
BRITISH POUND (1/24)	1.51	1.53	1.59
FRENCH FRANC (1/24)	5.08	5.00	5.25
ITALIAN LIRA (1/24)	1591.5	1582.3	1603.0
CANADIAN DOLLAR (1/24)	1.37	1.37	1.41
MEXICAN PESO (1/24)[3]	7.450	7.505	5.550

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

RETAIL SALES

Monday, Jan. 29, 8:30 a.m. ▶ Retail sales probably rose 0.6% in December, says the median forecast of economists surveyed by MMS International, one of The McGraw-Hill companies. Most of the strength will be in autos. Excluding vehicles, sales likely were up a mere 0.2%, helped by higher gasoline prices. In November, total sales rose 0.8%; excluding cars, they rose 0.9%.

FOMC MEETING

Tuesday, Jan. 30 ▶ The Federal Reserve's Federal Open Market Committee will meet to set monetary policy. The MMS forecast is that the federal funds rate will remain at 5.5%. The meeting will continue into Jan. 31.

CONSUMER CONFIDENCE

Tuesday, Jan. 30, 10 a.m. ▶ The Conference Board's index of consumer confidence was probably little changed in January from its reading of 98.7 in December.

FEDERAL BUDGET

Tuesday, Jan. 30, 2 p.m. ▶ The government likely had a deficit of about $5 billion in December, vs. $4.8 billion a year ago.

PRODUCER PRICE INDEX

Wednesday, Jan. 31, 8:30 a.m. ▶ Producer prices of finished goods likely increased by 0.4% in December, led by rising gasoline and natural gas prices. The PPI rose 0.5% in November.

CONSUMER PRICE INDEX

Thursday, Feb. 1, 8:30 a.m. ▶ Consumer prices likely rose 0.3% in December, after no change in November. As with producer prices, higher energy costs led the runup.

NAPM SURVEY

Thursday, Feb. 1, 10 a.m. ▶ The National Association of Purchasing Management's index likely fell to 45% in blizzard-impaired January, from 46% in December.

EMPLOYMENT

Friday, Feb. 2, 8:30 a.m. ▶ The MMS forecast calls for a job gain of 125,000 in January, after a rise of 151,000 in December. The jobless rate likely remained at 5.6%.

This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

BusinessWeek ONLINE

Monday

How do you pick the best mutual fund? Check out BW's Mutual Fund Scoreboard in this issue, ranking 885 equity funds by performance. And join a conference with Amy Arnott of Morningstar, which supplied the data, and BW's own mutual-fund maven, Senior Writer Jeff Laderman.

Jan. 29
9 p.m. EST in the Globe

Wednesday

For help in managing a business in an environment that often seems like chaos, talk with Bill Dauphinais, leader of the team who wrote *The Paradox Principles*, and BW's John Byrne, senior writer specializing in management topics. **Jan. 31**
9 p.m. EST in the Coliseum

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

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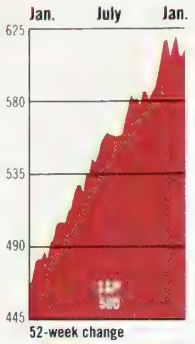
Business Week (ISSN 0007-7135) published weekly, except for one issue in January, by The McGraw-Hill Companies, Inc. Executive, Ed Circulation, and Advertising Offices: 1221 Avenue of the Americas, New York, N.Y. 10020. U.S. subscriber rate $49.95/year; Canada $69/year. Second-class postage paid at New York, N.Y., and at additional mailing offices. Postage paid at Montreal, P.Q. Canada Post Intern Publications Mail Product Sales Agreement No. 246484 **Postmaster:** Send address changes to BUSINESS WEEK. P.O. Box 430, Hightstown, N.J.

Investment Figures of the Week

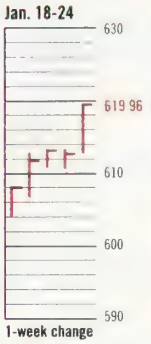
MMENTARY

. Dow Jones industrial average e to an all-time high of 5,243— .5% increase from a week ago. ong fourth-quarter earnings m IBM, Microsoft, and United hnologies helped lift the index. fear grew that the budget stale- te in Washington would lead to efault, the yield on the 30-year asury rose to 6.09%, but pped to 6.03% as the threat of ault waned. The deal of the k: Wells Fargo's announcement t it would acquire First Inter- te. Speculation grew that Apple nputer would be taken over.

STOCKS

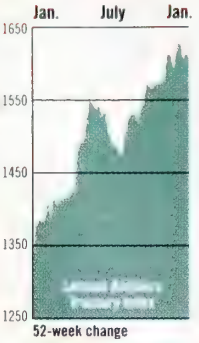


52-week change +32.6%

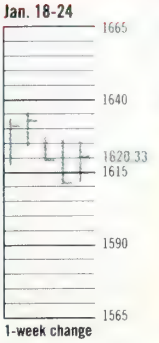


1-week change +2.2%

BONDS

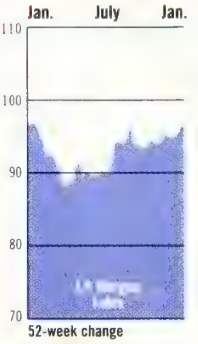


52-week change +19.7%

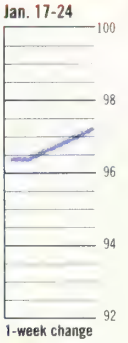


1-week change −0.3%

THE DOLLAR



52-week change +0.6%



1-week change +0.9%

MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
N JONES INDUSTRIALS	5242.8	3.5	35.4
SIZE COMPANIES (S&P MidCap Index)	216.9	3.1	26.5
ALL COMPANIES (Russell 2000)	310.4	2.6	24.8
COMPANIES (Russell 3000)	353.0	2.4	32.0
REIGN STOCKS	**Latest**	**% change (local currency) Week**	**52-week**
IDON (FINANCIAL TIMES 100)	3758.2	1.5	26.0
YO (NIKKEI INDEX)	20,312.7	−1.3	11.9
ONTO (TSE COMPOSITE)	4684.1	−1.9	14.1

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.12%	5.13%	5.93%
30-YEAR TREASURY BOND YIELD	6.03%	6.01%	7.86%
S&P 500 DIVIDEND YIELD	2.22%	2.27%	2.77%
S&P 500 PRICE/EARNINGS RATIO	17.3	17.1	16.6
TECHNICAL INDICATORS	**Latest**	**Week ago**	**Reading**
S&P 500 200-day moving average	568.0	565.3	Positive
Stocks above 200-day moving average	65.0%	64.0%	Neutral
Speculative sentiment: Put/call ratio	0.60	0.74r	Neutral
Insider sentiment: Vickers sell/buy ratio	1.50	1.45	Positive

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

6-MONTH LEADERS	% change 1-month	% change 12-month	Strongest stock in group	% change 1-month	% change 12-month	Price
DEFENSE ELECTRONICS	26.1	140.3	LORAL	30.7	137.1	44¾
GOLD MINING	15.3	36.9	SANTA FE PACIFIC GOLD	28.3	35.1	15⅞
HOTELS AND MOTELS	9.2	25.8	HILTON HOTELS	18.9	12.1	73⅛
STEEL	7.7	−6.2	USX-U.S. STEEL GROUP	9.9	−4.6	33⅜
RESTAURANTS	7.4	54.7	McDONALD'S	8.7	65.1	48½
6-MONTH LAGGARDS	**% change 1-month**	**% change 12-month**	**Weakest stock in group**	**% change 1-month**	**% change 12-month**	**Price**
SEMICONDUCTORS	−11.6	14.0	LSI LOGIC	−29.1	22.8	25¼
TRUCKING	−8.8	−13.5	CALIBER SYSTEM	−13.9	−15.2	36⅜
GENERAL MERCHANDISE CHAINS	−8.6	2.7	KMART	−17.2	−55.1	6
SAVINGS AND LOANS	−7.5	45.3	GREAT WESTERN FINANCIAL	−8.3	40.6	23⅜
MANUFACTURED HOUSING	−7.3	29.9	FLEETWOOD ENTERPRISES	−7.3	33.3	24

MUTUAL FUNDS

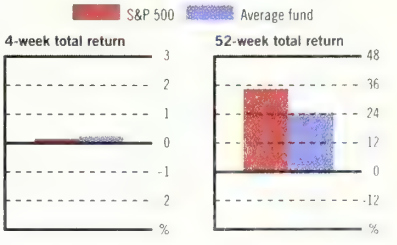
MORNINGSTAR INC

ADERS

r-week total return	%
MORGAN STANLEY INSTITUTIONAL GOLD	16.2
SCUDDER GOLD	15.7
DS PRECIOUS METALS A	15.5
week total return	**%**
ALGER CAPITAL APPRECIATION	70.5
FIDELITY SELECT ELECTRONICS	66.6
MIDAS	66.1

LAGGARDS

Four-week total return	%
GOVETT SMALLER COMPANIES A	−10.2
STEADMAN AMERICAN INDUSTRY	−9.9
TWENTIETH CENTURY GIFTRUST INVESTORS	−9.7
52-week total return	**%**
EV MARATHON GREATER INDIA	−34.1
STEADMAN AMERICAN INDUSTRY	−28.4
STEADMAN TECHNOLOGY GROWTH	−27.6



RELATIVE PORTFOLIOS

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Dollar amounts represent the present value of $10,000 invested one year ago in each portfolio

Percentages indicate 1-day total returns

U.S. stocks	Treasury bonds	Foreign stocks	Money market fund	Gold
$13,403	**$13,240**	**$11,932**	**$10,564**	**$10,441**
+0.71%	+0.05%	−1.21%	+0.12%	+1.52%

Data on this page are as of market close Wednesday, Jan. 24, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close Jan. 23. Mutual fund returns are as of Jan. 19. Relative portfolios are valued as of Jan. 23. A more detailed explanation of this page is available on request. r=revised

THE POLITICS OF STAGNATION

The state of the union is far more parlous than President Clinton's soothing speech would have us believe. Going into 1996, the vast majority who inhabit the sensible center of America are appalled at the elbows-out partisanship and polarization in Washington. The pettiness, the anger, the demagoguery are disgusting. The Washington scene is a caricature of a TV talk show, with sanctimonious politicians screaming past one another, forsaking accomplishment only to wallow in self-righteousness. Who voted for this?

It's wrong simply to focus on who is winning and who is losing. Thanks in part to a media culture that prizes celebrity over thoughtfulness, conflict over compromise, and ideology over pragmatism, political extremists of both parties are egged on to ever more bombast. Ridicule and exaggeration pass for explanation and context. The Democrats yell that the Republicans are out to destroy Medicare. The Republicans shout that the Democrats want to destroy the middle class with taxes. This kind of vulgar politics is doing great harm to America.

It is time to return to a political discourse of sense and sensibility, of respect and civility. There are no overwhelming political mandates in America that sweep away the need for negotiation and compromise. The 1994 elections did not signal a return to 19th century conservatism any more than the 1992 elections signaled a return to New Deal liberalism.

The most important issue is the one discussed least: growth. Fast, noninflationary economic growth, at 3%-plus a year, is the key to securing jobs, raising income, and providing resources for education and health. Yet most of the talk about balanced budgets, entitlements, Medicare, and taxes is really about defending existing franchises in an era of government downsizing and slow growth, be they health care for the elderly or subsidies for cattle grazers. The current deb is about how to survive the economics of stagnation, as terest groups vie for their "fair share" of finite resources

With the 1996 campaign under way, it is time to judge p cies—taxes, entitlements, research, education, and the anced budget—by their impact on economic growth. Taxes, example, should be cut and simplified to spur capital spend and reward individual work. Simply giving tax credits families for having children does little to expand the econo however welcome the extra cash may be. It would be far ter to cut income taxes.

Monetary policy must also focus on growth. The effort downsize government is already putting an enormous fis drag on the economy, which is crawling along at abou measly 1% to 2% rate. It will get worse once a bud deal is finally reached. Yet hard-liners in the Fede Reserve, obsessed with zero inflation, resist lowering terest rates. They want lower economic growth and hig unemployment to keep prices from rising. We believe t productivity is higher than official figures indicate and al for faster growth without more inflation.

If the economy doesn't grow at 3% a year, there is li hope of generating the resources people will need to well, raise children properly, and plan for their old age in 21st century. It may indeed be that the trashy tone in Am ican politics today results from huge fights over the dist ution of income in a static economy. Only through policies t promote investment in fast economic growth can the U.S. ally prosper. That's what the 1996 campaign should be about. Here's hoping.

THE LESSONS FROM APPLE'S DECLINE

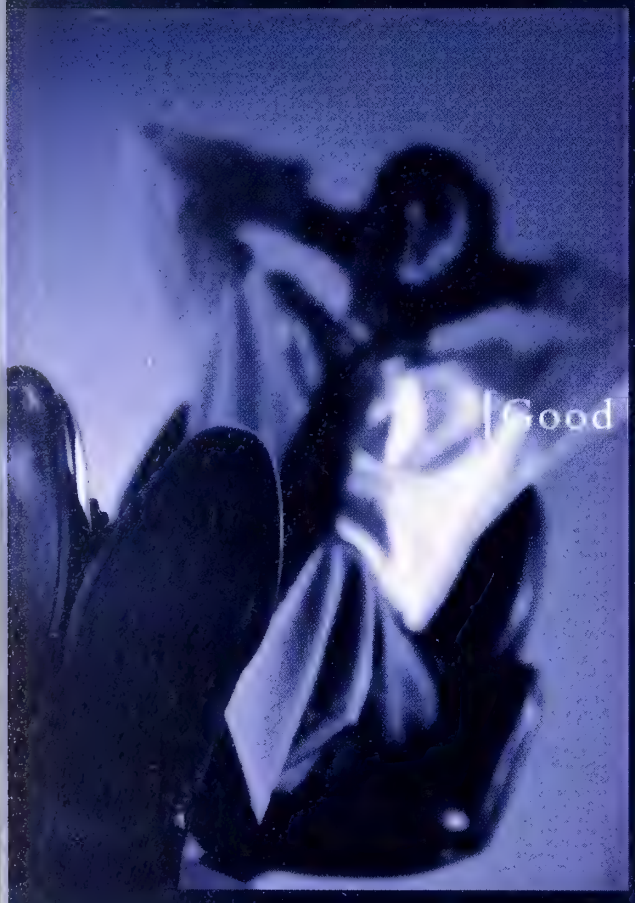
Remember when it was all so exciting? The Apple II that played all those games? The incredible Mac, with a dynamite graphic interface that did away with all those idiotic DOS commands? Remember playing with a mouse for the first time, trying to click onto the icons? There was so much magic in Apple Computer in the early '80s that it is hard to believe that it may fade away, folded into another computer company or surviving as a mere niche player. Apple transformed cold bits and bytes into cool tools and toys for millions of people around the world. Its decline is sad testimony that product innovation and bold vision are sometimes not enough for long-term survival. Apple went from hip to has-been in just 19 years.

In an entrepreneurial society, such as America, the lessons of Apple's decline are extremely important. Apple's core renegade culture planted the seeds of its demise. From the very beginning, the "creators" of technology held experienced managers and marketers in total disdain. They were corporate "suits," the enemies of the jeans-clad clique aro Steve Jobs that was defying the Establishment.

The result? An inward-looking, closed culture kept Ap from expanding into the larger marketplace. The orig Mac was underpowered and literally closed to non-Ap technology. It took the removal of Jobs by John Sculley open the Mac up. But Sculley, like Michael Spindler who lowed, could not persuade the techies to go further and lice the Mac operating system. Had Apple done so, it might h dominated the computer market around the world.

Instead, Apple remained aloof from the marketplace let its core technology stagnate. Microsoft Corp. has all caught up to it with Windows 95, and the rest is history. novation and vision could not compensate for hubris, w management, and a board of directors that let once-preci assets rot on the vine.

You don't really *want* to plan this meeting.



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MUTUAL FUNDS THE BEST BOND FUNDS

BusinessWeek

FEBRUARY 12, 1996

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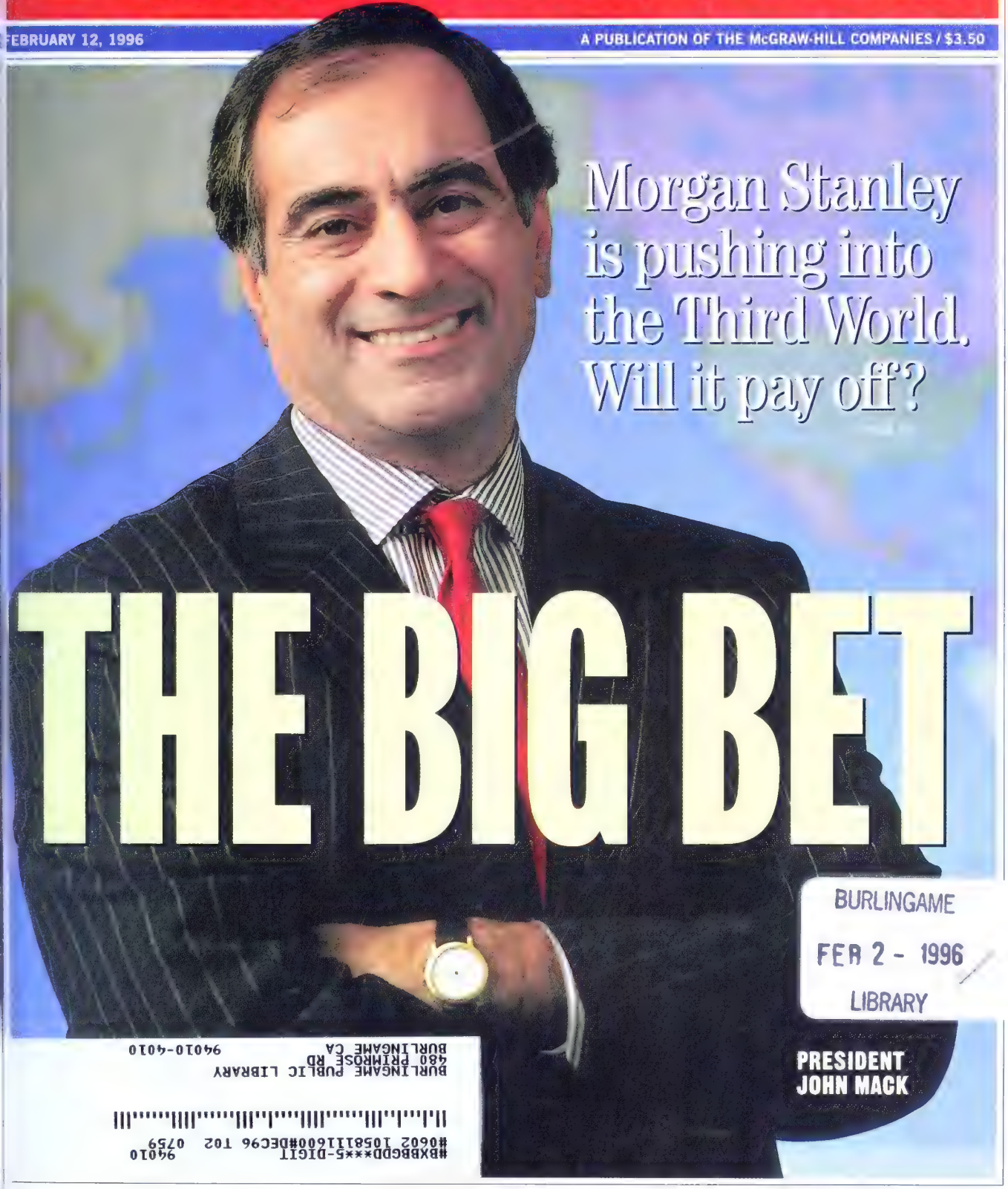

Morgan Stanley is pushing into the Third World. Will it pay off?

THE BIG BET

PRESIDENT JOHN MACK

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INTRODUCING THE ALL-NEW MERCURY SABLE WAGON

It used to be some stretch of the imagination to think a station wagon could ever deliver the ride, handling and comfort o a sedan. But now it's as simple as imagining yourself in the all-new 1996 Mercury Sable wagon. Sable wagon has a lot i common with Sable sedan — the incredible feeling of solidity, the rewarding and precise road manners and an engine tha goes 100,000 miles between scheduled tune-ups.* But Sable wagon adds a few twists of its own, like an available rear-facin

Imaginatio

Sable's all-new 3.0L Duratec V6 produces 200 horsepower.

All Sable engines go 100,000 miles between scheduled tune-ups.*

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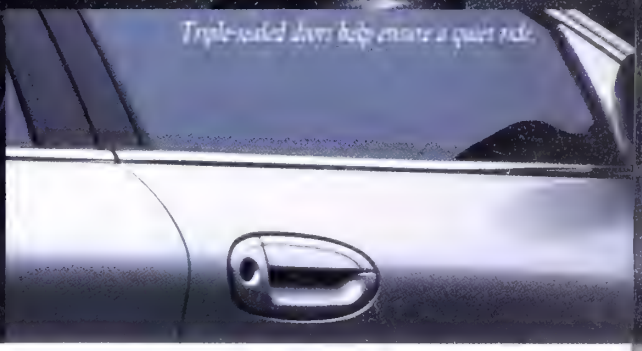

Triple-sealed doors help ensure a quiet ride.

Mercury Sable LS Wagon

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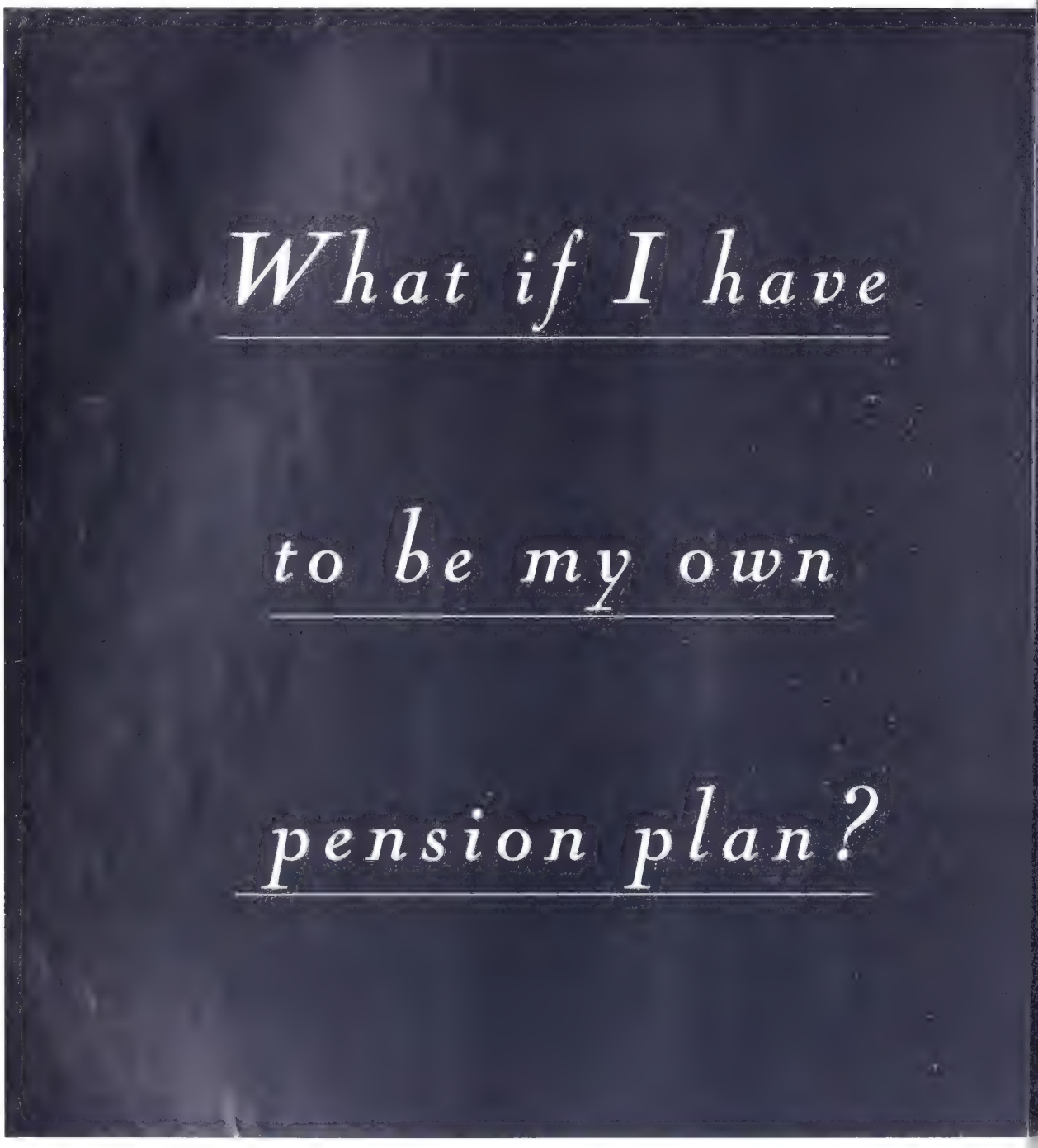

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BusinessWeek

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Do the deal now

Up Front

TALK SHOW "This election is not for sale. It doesn't go to the highest bidder."

—Senator Bob Dole (R-Kan.), sniping at his free-spending GOP rival, Steve Forbes

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

THE FEDS

AN UNLIKELY PLACE FOR A BIAS CHARGE

COMMERCE SECRETARY RON Brown, the highest-ranking black in the Clinton Administration, is taking heat on diversity. Despite Brown's attempts to improve his agency's affirmative action performance, a black Commerce employees group has filed race and gender bias complaints with the Equal Employment Opportunity Commission.

BROWN: *Zapped on diversity*

And now, the Commerce Committee for African American Concerns has done a study that finds blacks make up 18% of the department's 33,000 staffers yet less than 7% in the middle and high civil-service levels, GS-7 and up. It says Commerce ranks 38th out of 58 federal agencies in the share of black professionals and 47th for female professionals.

The Commerce Dept. calls the numbers, which come from 1994, outdated. While it produces no overall figures to fire back with, it notes that the number of minorities and women who are in top management, called the Senior Executive Service, rose by one-third during a 17% overall decline of such workers.

And not all black employees are displeased with the Commerce Secretary. The American Federation of State County and Municipal Employees issued a 1995 report card on Brown that awarded him an "A-plus in everything," says Anita Sanders, president of AFSCME Local 3810, one of 12 unions at [illegible]rce. *Catherine Yang*

GETTING ON: *Medicare is 30*

TAXES AT WORK

A WINDFALL FOR OLD GRINGOS?

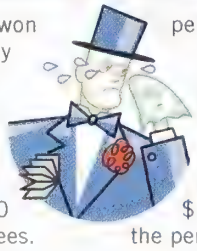
CALL IT THE EXPATRIATE subsidy. The Republicans' budget proposal would grant the 335,000 American retirees living abroad a hunk of cash via Medicare. These folks, many of them well-off, now receive $1.8 billion a year in Social Security but nothing in Medicare benefits. Reason: Only U.S. doctors are eligible for Medicare reimbursements.

GOP lawmakers want to revamp Medicare, now 30 years old, by giving each new retiree about $5,000 if they agreed to use some of it to buy individual catastrophic health coverage, which runs about $3,000 a year. The remaining $2,000 goes into so-called Medical Savings Accounts, to pay the catastrophic policies' high deductibles.

But retirees who move abroad could take the $5,000 payment, buy an insurance policy to please Uncle Sam, and, say critics, pocket the $2,000. How? By taking advantage of the free health care many countries offer.

That's why Democrats call the scheme wasteful, costing $770 million extra yearly. Republicans say the plan will save money overall by making retirees prudent health-care shoppers. *Paul Magnusson*

THE LIST **COSTLY ROMANCES**



Wells Fargo has won First Interstate away from its intended merger partner, First Bank System. But the rebuffed suitor gets a consolation prize—a record $200 million in breakup fees. Popular since the '80s, these fees compensate a spurned partner for its expenses. One sticking point between Hasbro and Mattel before talks ended: the fee's size, with Hasbro's wanting at least double Mattel's $100 million offer. If the pending Time Warner-Turner union fizzles, Time Warner will get a sweet $175 million for its troubles.

LARGEST MERGER BREAKUP FEES PAID

TARGET	THWARTED ACQUIRER	DEAL ENDED	FEE MILLIONS
FIRST INTERSTATE	FIRST BANK	1996	$200
UAL	MANAGEMENT, PILOTS' UNION	1989	80
LIN BROADCASTING	BELLSOUTH	1989	54
ALLIED STORES	EDWARD DeBARTOLO, PAUL BILZERIAN	1986	53
GRUMMAN	MARTIN MARIETTA	1994	50
FEDERATED DEPT. STORES	R.H. MACY	1988	45
LEAR SIEGLER	WICKES	1986	30
KEMPER	CONSECO	1994	30

DATA: SECURITIES DATA CO

OVER THERE

TEARDROPS ON THE SHELVES

WHO IS KILLING THE GREAT old stores of Europe? Discounters, hypermarkets, and other low-cost operators. Traditional retailers in the U.S. got whacked by this phenomenon several years ago as consumers cut back on full-price places in favor of Wal-Mart Stores and the like. Also troubling the European retail establishment is a slowing economy. The losers are both the grand old department stores and the corner shops known more for their convenience than their prices.

France's venerable Galeries Lafayette says it will shut 5 of its 22 French department stores and lay off more than 1,000. Switzerland's Jelmoli chain has decided the business has no future and wants to put 34 of its 35 department stores on the block. In Italy, Marco Venturi, head of retailer association Confesercenti, sees 10,000 small stores going under every year until decade's end.

ADIEU: *Five stores closing*

Big hypermarket chains, such as France's Carrefour and Promodès, are bringing this on with their relentless cross-border march. So are a bevy of specialty chains: Gap, Toys 'R' Us, and Foot Locker from the U.S., British food and apparel retailer Marks & Spencer, and Swedish furniture chain Ikea. Reminiscent of the American retail situation, they're all rushing to the suburbs, where property costs are lower. *Stewart Toy*

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AMERICAN EXPRESS Cards

Up Front

HONCHOS

IF THE PAY'S THE THING, JUMP SHIP

PAYING YOUR DUES LOOKS less and less appealing. It has long been true that CEOs brought in from the outside get bigger pay hikes than those promoted from within. But now the difference is growing wider.

EXTERNAL HIRES

	OLD PAY	NEW PAY
	IN MILLIONS OF DOLLARS	
CHARLES HARPER	$1.27 *ConAgra*	$2.45 *RJR Nabisco*
JERRY DEMPSEY	$1.01 *Chemical Waste Mgt.*	$2.00 *PPG Industries*

INTERNAL PROMOTIONS

PHILIP FLETCHER	$1.12 *ConAgra*	$1.23
WALTER SHIPLEY	$2.25 *Chemical Bank*	$2.49

DATA: COMPANY REPORTS, BUSINESS WEEK

The gap averaged 13% in the 1980s, according to a recently released Wharton School study of CEO salaries and bonuses. In the early 1990s, as companies reorganized for tougher global competition, that figure climbed to 15%, says headhunter Jerry Simmons at Handy HRM. Today, he estimates, it's between 20% and 30%, a figure that executives at other search firms agree with. Many headhunters believe the differential will widen even more in coming years, especially through increased use of stock options.

The reason for the gap is that outside stars cost more. Says University of California at Berkeley Professor Graef Crystal: "If you ask a recruiter to find a CEO, he is going to bring you an ace or king. If you recruit from within, you are going to get a seven or eight."

When CEO Charles Harper left ConAgra to take the top job at RJR Nabisco in 1993, he almost doubled his pay. His replacement from within, Philip Fletcher, got a not-so-princely 10% raise (table). □

SICK PLANET

A CHOKE HOLD IN MEXICO CITY

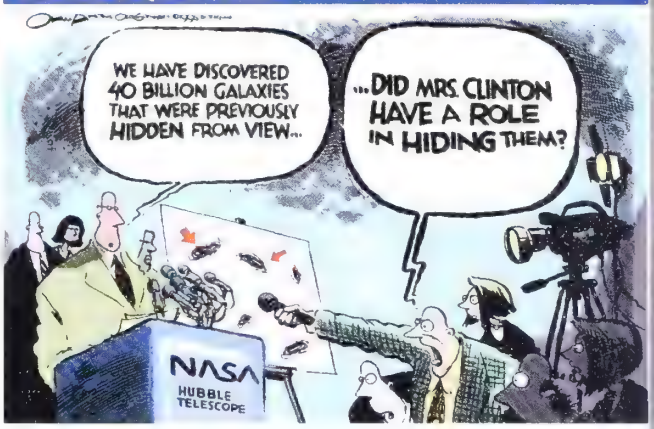
AS IF MEXICO'S SLUMP WEREN'T bad enough: Air pollution is taking an additional bite out of the economy. For years, residents of Mexico City have resigned themselves to winter respiratory problems when the weather traps bad air in the valley metropolis. But now, pollution counts are reaching nearly three times the maximum acceptable level.

So city officials recently took emergency measures, forcing even industries with pollution controls to cut production by 30% to 40%. And for the first time, the city required people to keep their cars off the street for three days a week. The measures were lifted after four days, when levels drifted down to 180% of the standard. Yet the curbs may soon be reimposed, as more bad smogouts are expected. Autos account for 70% of the pollution.

Environmental and business groups estimate that the measures cost companies about $5 million a day—not counting lost productivity from worker absenteeism. While many polluters have moved away in recent years, such major ones as glass and paper makers remain. The city still accounts for 24% of Mexico's industrial output. *Geri Smith*

SELLING WELL: *Filter masks*

DRAWN & QUARTERED



SHOW BIZ

THANKS FOR THE PLUG, I GUESS

GUESS WHAT, *SEINFELD* FANS: Elaine's self-important, windbag boss has a real-life counterpart. Last season, the hit NBC sitcom (No. 2 in the ratings) introduced the silver-haired J. Peterman, head of an eponymous apparel catalog, who drives Jerry Seinfeld crazy by reciting Hemingwayesque descriptions of his upscale goods. Example: He ran with the bulls at Pamplona in his "Italian captoe Oxfords—sophisticated yet different."

The real J. Peterman heads the Lexington (Ky.)-based J. Peterman catalog, whose copy is a lot like the character's lines, although not as wacky. Newest item: a sweater worn by a woman fans will recognize as Elaine.

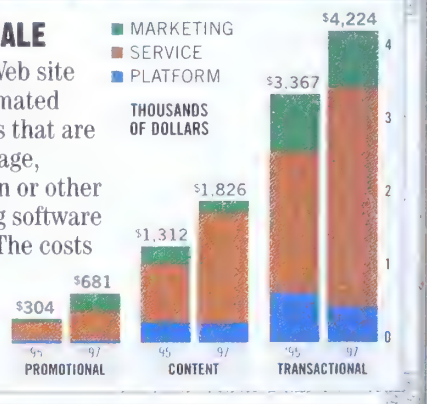
Peterman says NBC contacted him about using the character only after he appeared. The network says the exposure is good for the mail-order man and that Seinfeld is a customer. Peterman (first name: John), who doesn't know if sales have benefited, takes it all in stride, but says: "I'd like to believe I'm not a bore." *Lori Bongiorno*

***SEINFELD** and the real Peterman, right*

THE BIG PICTURE

WEB SITE FOR SALE

How much does a Web site cost? Here are estimated costs for companies that are promoting their image, offering information or other content, and selling software or other products. The costs assume a site that starts in 1995 and keeps growing.



DATA: FORRESTER RESEARCH INC.

FOOTNOTES Percentage of Americans who believe 100 CEOs could run the country better than 100 politicians: 36%

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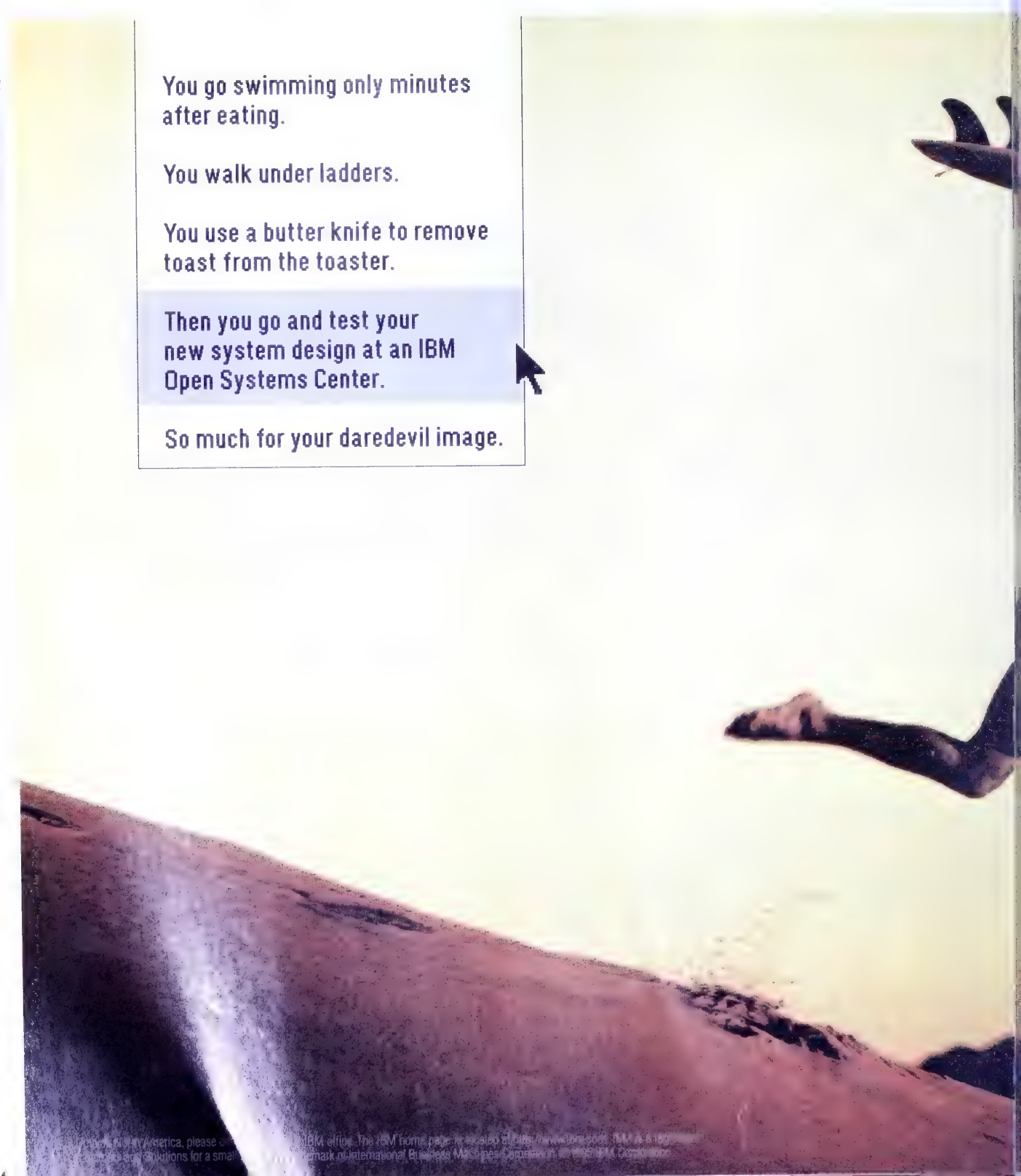

Even those who live on the edge know they shouldn't take chances when designing a client/server system for their business. With so much to be gained, you have to be sure that everything goes just right.

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Readers Report

WHY THE FAA CERTIFIED BOEING'S 777

In response to your question "Did the FAA go easy on Boeing?" (The Corporation, Jan. 29), the answer is an emphatic no. No aircraft in history has undergone FAA testing as comprehensive and thorough as the Boeing 777. Nearly 90 Federal Aviation Administration engineers spent more than 125,000 hours certifying this plane—over twice as long as any previous aircraft.

The decision to certify the 777 was based on scientific data and on extensive testing of the entire aircraft. Your article relied on documents from various stages of the process that were inaccurately portrayed as final documents. These documents represent the give-and-take that is critical to resolve certification issues.

It should also be noted that certification of the 777 was an effort coordinated by the FAA and the Joint Aviation Authorities, an organization representing 23 European bodies. The JAA, using the same data as were provided to the FAA, arrived at the same conclusion: that the 777 is safe to fly.

David R. Hinson
Administrator
Federal Aviation Administration
Transportation Dept.
Washington

BUSINESS WEEK has done the traveling public and the aerospace industry a disservice. The certification process is an extremely complex one, which the reporter apparently did not understand or decided to ignore. Your reporter chose selected data from this complex process and made them appear to be the whole process. Your reporter used anonymous and unidentified sources to corroborate her theory.

Prior to entry into service, the Boeing 777 had been more thoroughly tested than any jetliner ever produced. During the certification process, Boeing cooperated fully in conducting the most rigorous laboratory, ground, and flight-testing program in the history of commercial aviation. We stand behind the safety and reliability of our products.

Ronald B. Woodard
Boeing Commercial Airplane Group
Seattle

CORRECTIONS & CLARIFICATIONS

"The Fed: Frozen in time" (Up Front, Jan. 22) incorrectly listed the new name for Kemper Financial Services. It is Zurich Kemper Investments.

"Wal-Mart: A string snaps" (In Business This Week, Jan. 29) should have said the retailer was expected to earn $970 million for the fourth quarter, not $97 million.

"Don't leave your broker without it?" (Inside Wall Street, Feb. 5) said that American Express Co. posted disappointing yearend results. Earnings, though, were only 1% below the consensus forecast. And only one analyst cut his 1996 and 1997 estimates. Still, the stock dropped on the earnings announcement.

SWIMMING WELL IN A BIG POND

I would like to correct and clarify points made in "What's this little fish doing in such a big pond?" (News & Analysis & Commentary, Dec. 25) about U.S. Enrichment Corp.'s selection of our firm as one of the co-managers for its potential privatization offering.

M. R. Beal & Co. maintains the equity-research capability that would be required to follow U.S. Enrichment paper in the secondary market. It has extensive relationships with floor brokers on all major exchanges. It is fully approved by and currently doing business with the Resolution Trust Corp. and other federal, state, and local government agencies. And our firm made a superior presentation to U.S. Enrichment.

We pride ourselves on being professional and competent, and we seek out only business that we believe we can successfully execute on behalf of our

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FEBRUARY 12, 1996 (ISSN 0007-7135)*** 3462

Published weekly, except for combined issues in January by The McGraw-Hill Companies, Inc. Founder: James H. McGraw (1860-1948). Executive, Editorial, Circulation, and Advertising Offices: The McGraw-Hill Companies Building, 1221 Avenue of the Americas, New York, N.Y. 10020. Telephone: 212-512-2000. Telex: Domestic 127059 Int. 236012576. One subscription rate $42.95 per year. 2 years $70.00, 3 years $89.95. Single copy $2.50. Outside the U.S. Write for rates in other countries. Subscription Services: 1-800-635-1200 (TDD: 1-800-554-1570).

Postmaster: Send address changes to BUSINESS WEEK, P.O. Box 430, Hightstown, N.J. 08520. Second class postage paid at New York, N.Y. and at additional mailing office. Postage paid at Montreal, P.Q. Canada Post International Publications Mail Product Sales Agreement No. 246484.

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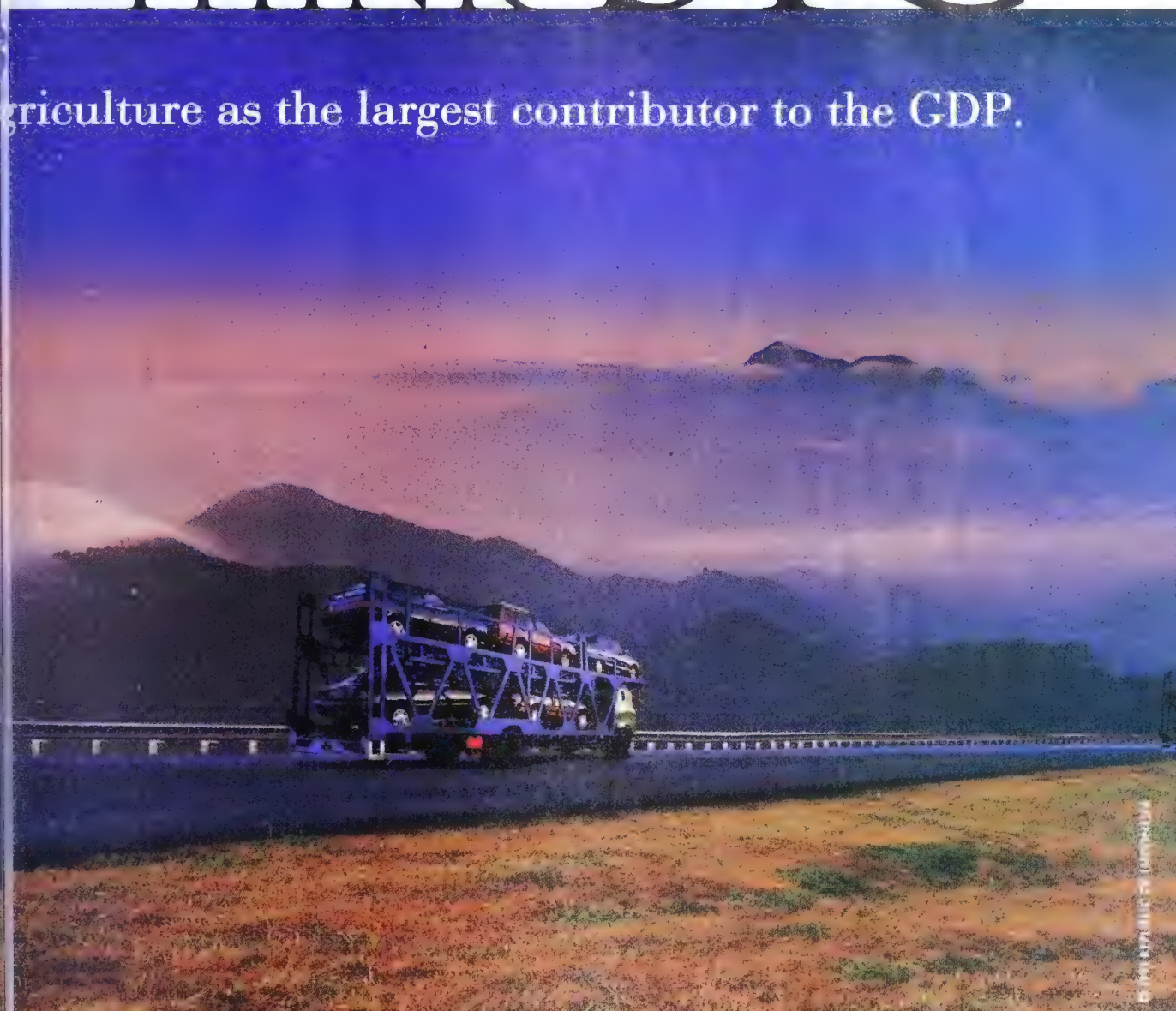

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clients. Readers of your story might have been given a different impression by comments by people expressing "sour grapes" whom we beat in competition for a piece of business.

Bernard B. Beal
Chief Executive Officer
M. R. Beal & Co.
New York

VENEZUELAN INVESTING, REVISITED

Regarding your article on Venezuelan mining, "Between a nugget and a hard place" (Letter from Venezuela, Jan. 22), I must inform you that the quote attributed to me—"If I had the choice, I would never invest again in Venezuela"—does not reflect my personal beliefs on investing in Venezuela, nor those of the company I represent. Furthermore, I never use the first person singular in speaking about such matters.

I am a Venezuelan citizen born and raised here, with the majority of my personal investments in this country. Anyone who knows me knows that I am a hopeless optimist and I am for development of mining in this country. As such, I am a director of the Venezuelan Mining Chamber, which is dedicated to the promotion and development of modern mining in Venezuela. Further, our company has made investments in excess of $20 million in this country with outstanding early geological results. The results have been so encouraging that Bema Gold has chosen a strategy for this year that allows us to commence a prefeasibility drilling program with the objective of proving the presently delineated geological resource of 850,000 ounces, in order to bring this deposit into production at the earliest possible time.

Courtney Neeb Brewer
President
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SUN'S McNEALY: A MODEL FOR AMERICA?

In "Scott McNealy's Rising Sun" (Cover Story, Jan. 22), you offer a wonderful portrait of much that is unique to America. McNealy's accomplishments at Sun speak volumes to the fact that—as we approach the dawn of a new century—the American dream is alive and well. I hope his modern-day story and the outstanding coverage you gave it will inspire many, many more as they struggle to make their own dreams come true.

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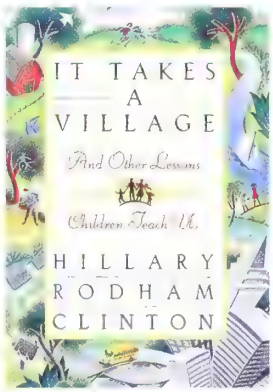
IT TAKES A VILLAGE
And Other Lessons Children Teach Us
By Hillary Rodham Clinton
Simon & Schuster • 318pp • $20

HILLARY'S 300-PAGE CAMPAIGN SPEECH

Let's try to forget for a moment that there's an election looming, that Bill Clinton doesn't quite have it locked up, that the endless Whitewater circus continues to expose the First Couple's, um, inconsistencies, and that Hillary Rodham Clinton's standing among the masses is not what it once was.

Nope. Just can't do it. The ugly political realities persist. Which is why Hillary Clinton's *It Takes a Village* comes off as among the most cynical publishing undertakings in recent memory.



Here is how things appear: The First Lady, or someone, selected the most unassailable stand available—that we should treat our children better—then penned a 300-page campaign speech. (It's best to be cautious on the question of authorship, actually. The White House insists that the work is Hillary Clinton's and is trotting out handwritten chapter drafts to prove it; others say Barbara Feinman, former aide to several *Washington Post* honchos, helped a lot.)

This speech is appropriately facile and inoffensive, which is disappointing given Clinton's many years of serious work with children's advocacy groups. (Example: "The teenage years, we all know, pose a special challenge for parents.") It offers geographically and socioeconomically balanced, real-life anecdotes at every turn and drops copious reminders of the Family & Medical Leave Act, Early Head Start, and other youth-related initiatives credited to the Incumbent-Candidate.

It Takes a Village: The title derives from the currently fashionable African saying, "It takes a village to raise a child." Not once in my two years in Africa did I hear this maxim, but the essence is credible enough. Many villages are indeed characterized by a strong sense of collective responsibility for all their people, but especially for infants, the infirm, and the elderly.

Clinton argues that comparable social structures in America have withered: Communities whose citizens look out for each other have been fractured, and extended families have dispersed. "There are fewer Aunt Belles, grandparents, and other relatives close by, and many of us no longer feel free to ask a neighbor to lend a hand or an ear," she writes.

The First Lady proposes a new sort of village, an amalgam of family, friends, neighbors, business, government, and, well, everyone. This village must instruct new mothers, help with child care, improve education, assure medical care, and keep kids safe. The village must do a lot. Readers quickly will tire of the word village.

It is a measure of this book's political aspirations that Clinton promulgates this overarching consortium while at the same time proclaiming her belief in the need for self-reliance. "Parents bear the first and primary responsibility for their sons and daughters," she writes. The community, not least its government, is obliged to help—but individuals ultimately make the beds their children will sleep in.

In principle, I agree—but this finely calculated ambivalence is disturbing. The First Lady manages to remain more or less true to her liberal past, while playing to a nation warming quickly to the idea that it doesn't need so much government after all. She condemns conservative extremists who argue "against the basic protections government extends to the well-being of individuals, families, and communities." Make no mistake, though: Extremists blew Democrats away in 1994, and the White House isn't bold enough to write them off now.

Clinton's assessment of business—a village denizen with the bucks to make things happen—appears to be just as tenuous. She boasts of an economy "on a roll again," with more than seven and a half million new jobs created in her husband's Presidency. But large companies, driven to satisfy investors and "justify executives' high salaries," have embraced restructuring and layoffs with a vengeance. Too often, they "view most employees as costs, not investments," dedicating ever fewer resources to training, profit-sharing, family-friendly policies, and shared decision-making. Not like in the good old postwar days, she notes, when employers cared about creating jobs and lifting incomes.

The analysis is, to say the least, simplistic revisionism. Employers shell out far more today per worker on training, child care, and the like than they would ever have dreamed of spending in the 1950s. While some restructurings are indeed little more than hastily conceived nods to Wall Street, many others truly do help companies stay in business. And staying in business is profoundly family-friendly.

All that said, let us acknowledge where Clinton is, in fact, unassailable. We are neglecting too many of our children. Too many parents are incapable of caring and providing for their kids; too many, also, are unwilling. Traditional community support has broken down. Poor children get inferior food, day care, and schooling. Federal budget cuts inevitably will leave those children even worse off. And business should play a role in filling the void.

If this is true, why do I remain so offended by *It Takes a Village*? Because its author waffles, glosses, and pirouettes around solutions. Because she offers mass-market sound bites instead of the intelligence she clearly has. And because she has turned a credible cause into an insta-book, a vote-winning device. I'm betting it doesn't work.

BY KEITH H. HAMMONDS

Hammonds directs BUSINESS WEEK *coverage of social issues.*

THIS BE-NICE-TO-KIDS TOME IS AMONG THE MOST CYNICAL BOOKS IN RECENT MEMORY

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BY PAUL M. ENG

UPGRADER BEWARE

Installing a souped-up CPU may be more trouble and expense than it's worth

I've been happy with the performance of my two-year-old 486 PC for word processing. But lately, I've noticed that it slows to a crawl when trying to run some of the more demanding multimedia software. I had longingly been looking at ads for individual microprocessor chips you can buy to speed up your PC. In recent months, I saw prices for these chips fall rapidly and thought maybe it was time to upgrade my PC. With some of the chips going for as little as $130, it certainly seemed a lot cheaper than spending $2,500 for a new Pentium machine. Swapping out a processor couldn't be all that hard, right? Wrong.

First, you need to know which upgrade chip is right for your particular setup. Pentium-class CPUs are available and attractive because they are particularly well-suited to multimedia applications. But not every PC's main circuit board—or motherboard—can handle those chips. My Gateway 2000, for example, would have needed a new motherboard because the Pentium would be larger and more powerful than my 486. That would have been expensive (table).

Another factor to consider is the PC's BIOS (Basic Input/Output System) software. This describes each component in a computer and how it interacts with every other. If it is out of date, the BIOS will not recognize the faster processor upgrade. You may be able to get free BIOS upgrades from your PC maker or for about $80 from vendors such as Micro Firmware Inc. (800 767-5465). For information about your PC's motherboard and BIOS, it's best to check the manuals that came with your PC or call your PC maker. Your PC maker should also be able to tell you the maximum speed upgrade your system can safely handle.

For my PC, I chose a new chip called the Turbo Chip 486/133, whose "clock speed," or heartbeat, runs at 133 megahertz. That's much faster than the 33 Mhz on my Gateway. The TC486 series is designed by Advanced Micro Devices Inc. and sold by Kingston Technology Corp., a vendor well known for PC memory upgrades. I paid $140 for a kit that included a shoehorn-like chip-removal tool, a 40-page manual, and software to check out an upgraded computer. Swapping CPUs was a simple 15-minute process. Unfortunately, the chip didn't seem to work, which means my Gateway is unusable. Kingston is looking at the machine to figure out what happened, but I think I might have damaged the micro-thin circuits on the motherboard when I pulled the old processor out. Computer chips and boards are sensitive items. Handle with care.

ROADBLOCKS. I managed to install a new chip with no problems in an IBM ValuePoint PC provided by Kingston. Initially, I was impressed. Windows launched in 10 seconds, compared with 15 seconds with my old 486/33 Mhz chip. But according to a popular benchmarking program that measures speeds of performing various software functions, the TC486/133 was 4.21 times as fast as a 386DX/20. Impressive? Not really. A 486/33 Mhz turns in a score of 2.58. In other words, even though the TC486/133 is running four times faster than a regular 486/33, the performance gain is less than double. Obviously, simply upgrading your CPU cannot speed up other factors, such as how fast your hard drive works.

I learned the hard way that for most of us, upgrades are generally not worth the trouble and expense. I would recommend them mainly for the tinkerers who are confident of their abilities in fiddling with the innards of the PC.

Is Your PC Worth It?

What it might cost to soup up a 486 PC

ITEM	COST
[illegible]	$130-$300
BASIC INSTRUCTION CODE*	$0-$80
[illegible] MOTHERBOARD	$300-$800
TOTAL COST	$130-$1,180

*If necessary

DATA: BUSINESS WEEK

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HARDWARE

CEO, PHONE HOME

It's not Maxwell Smart's shoe phone, but it certainly could change our excuses for not keeping in touch with the home office. COMSAT Mobile Communications, a division of COMSAT Corp., recently introduced its Planet 1 personal satellite communications system. The 6-lb. device looks like a laptop computer. But open it, and a panel connects with an orbiting satellite to let you place and receive telephone calls from anywhere in the world. Fax, data, and paging services are also expected to be carried over the digital Planet 1 system. The $2,995 Planet 1 terminals will go on sale by mid-year. Calls will cost about $3 per minute.

SOFTWARE

FACE-LIFTS FOR WIN95

Windows 95 is barely six months old, and already software makers are clamoring to provide a new look. Successful programs such as Symantec Corp.'s Navigator and Starfish's Dashboard for the old Windows 3.1 operating system have migrated over to the new Windows. Now joining the fray is MicroHelp, with a utility called PowerDesk. Like its competitors, the $50 PowerDesk simplifies oft-used functions, such as file searches and floppy disk formatting, to a single mouse click.

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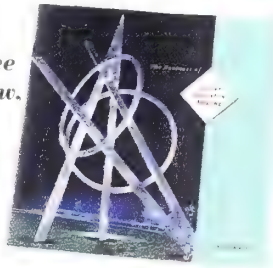

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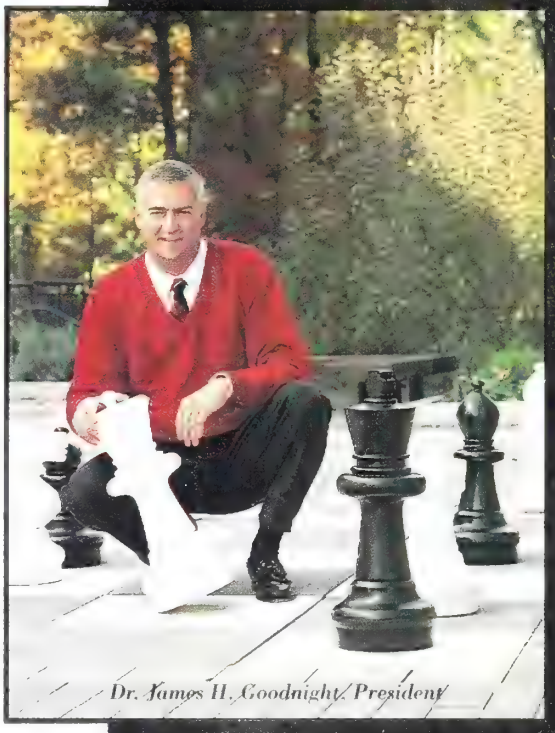

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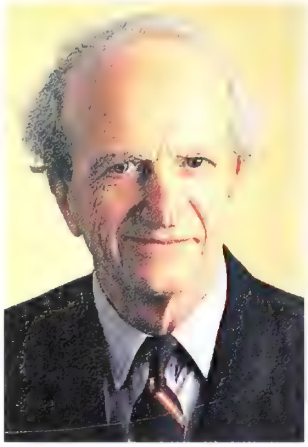
BY GARY S. BECKER

A FLATTER TAX JUST MIGHT KEEP FICKLE TEAMS AT HOME



INCENTIVE: High taxes beget tax-free municipal bonds. And muni bonds let cities build costly public stadiums to lure teams

Gary S. Becker, the 1992 Nobel laureate, teaches at the University of Chicago and is a Fellow of the Hoover Institution

The bitter controversy over the plan of the Cleveland Browns pro football team to move to Baltimore—after several decades on the shores of Lake Erie—reveals the fierce competition in the bidding for major league sports franchises. This competition is of concern to more than just the residents of the cities involved in the bidding wars, because taxpayers elsewhere help pay the bill.

Other taxpayers have a financial interest since part of the cost of stadiums, new roads, and other facilities is financed with municipal bonds that are exempt from federal income taxes. My colleague at the University of Chicago, Casey Mulligan, has calculated the expected cost of the fight going on between Chicago and the nearby city of Gary, Ind., for the Chicago Bears—one of the most prestigious sports franchises. Although it is unlikely that the Bears will decamp for Gary, the threat has forced Chicago Mayor Richard M. Daley to promise to spend almost $200 million to upgrade the stadium where the Bears have been playing, city-owned Soldier Field. Gary, for its part, has offered to spend much more to build a new stadium and roads and other facilities.

Both sides plan to raise some of their funds from tax-exempt municipal bonds. Long-term, top-quality tax-exempt munis now carry an interest rate well under 6%. If the Bears had to finance a new stadium or improvements themselves, they would have to pay much higher interest rates. Therefore, the victorious city saves millions of dollars in annual interest payments because a local government, rather than the Bears, owns the stadium where the team plays.

MULTIPLE OCCUPANCY. Mayor Daley claims that the upgrade of Soldier Field would not cost Chicago taxpayers anything. He says higher revenue to the city from rental payments by the Bears and greater spending by the public would cover interest payments on the additional city bonds. Whether or not he turns out to be right—and such forecasts are usually too rosy—remodeling by the city rather than by the Bears means less income-tax revenue for the U.S. Treasury, because munis are involved.

When baseball's Brooklyn Dodgers moved to Los Angeles in 1958 to begin the musical-chairs contest among local governments for sports franchises, almost all stadiums used by major league sports teams were privately owned. Often the football and baseball teams shared premises: The Chicago Bears, for example, then used the still-private Wrigley Field, home of the Chicago Cubs. Now almost all major football and baseball teams, and a majority of basketball and hockey teams, play in publicly owned stadiums.

The National Football League and Major League Baseball especially have taken advantage of the intense competition among local governments for their teams to demand separate stadiums funded with public money. These plush centers are usually bad investments. They are too large, too luxurious—and vacant practically all the time: Even big-league baseball teams play only 81 games at home. Private indoor arenas, such as the United Center in Chicago, keep down their costs by obtaining several teams, preferably major league hockey and basketball teams.

HOME LOYALTY. Franchises that own their stadiums and other specialized facilities also are less inclined to pick up and go to another city. That's because specialized sports facilities have little market value without a major league team playing there. The growth in government-owned stadiums is contrary to the trend toward privatizing garbage collection and other government services. Even Indianapolis, which has probably done more privatizing than any other city, continues to own the RCA Dome, home to the Indianapolis Colts football team.

Expansion of the market for lower-interest municipal bonds, especially tax-free munis, has made it possible for cities to compete for franchises by building uneconomic government-owned stadiums. The gap between interest rates on tax-free munis and comparable taxable bonds depends on the level of taxation and the degree of progressivity in the income-tax structure. People in high tax brackets, who have the most incentive to own tax-free bonds, bid down interest rates on munis so that their returns are comparable to yields on taxable bonds.

If Congress and President Clinton can agree on tax reform that has a much flatter income-tax schedule, the market for tax-free assets will decline. This will reduce the incentives of local governments to compete for sports franchises by offering to build new stadiums, and it will help return stadiums to private hands—where they belong.

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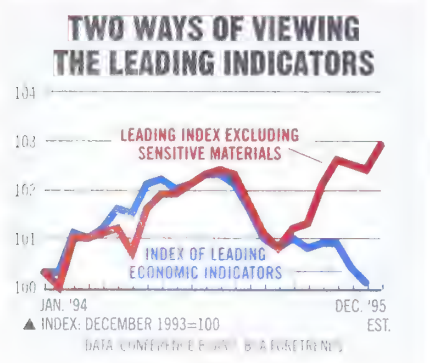
BY GENE KORETZ

AN OLD INFLATION SIGNAL FAILS...

Commodity swings can mislead

Economists have long considered commodity prices a critical economic indicator—providing perhaps the earliest signal of inflationary surges and strengthening business activity. Indeed, the Federal Reserve is known to keep a weather eye on gold and industrial materials prices as a clue to brewing inflationary pressures. And of the 11 components making up the index of leading indicators, the prices of sensitive industrial materials carry the most weight.

Commodity prices command this kind of attention, of course, because they are more flexible and volatile than other prices, responding rapidly to shifts in supply and demand. In a new Federal Reserve Bank of New York study, however, economists S. Brock Blomberg and Ethan S. Harris conclude that commodity prices have recently lost much of their power as predictors of inflation. Indeed, they find that since 1986 many commodity indexes have often given false signals—picking up steam in advance of actual slowdowns in inflation.



Why have commodity prices lost their ability to anticipate inflation? The researchers cite such trends as the Fed's readiness to step on the monetary brakes at the first hint of inflation, the impact of fluctuating exchange rates on dollar prices of internationally traded commodities, and the changing composition of U.S. output. Consumption of spot commodities, they note, fell from 8% to 10% of nominal gross domestic product in the 1970s to 4% by 1986. And with final demand shifting toward such sectors with low commodity content as services and electronics, such consumption may be even lower today.

Given these trends, Blomberg and Harris think that commodities will likely continue to diminish in importance as a measure of inflationary pressures and broad-based strength in the U.S. economy. However, even if they do poorly in predicting inflation in individual countries, they write, "commodity prices should retain some role as an indicator of global excess demand and a predictor of global inflation."

...BLURRING THE ECONOMY'S PATH

Materials prices skew a key index

If commodity prices are losing their power to predict inflation, what of their power to foretell the direction of economic activity? Recently, economist Warren C. Smith, who edits *BCA Credit ForeTrends*, a Bank Credit Analyst Research Group publication, looked at the behavior of the sensitive-materials component of the index of leading indicators.

Smith found that sensitive-materials prices, which have historically moved in tandem with other components of the index, diverged dramatically in 1995. In fact, they have been plunging since the middle of last year while the rest of the index has been strengthening. And because sensitive materials account for some 40% of the index, far outweighing any of the other 10 components, they have been dragging the rest of the index down (chart).

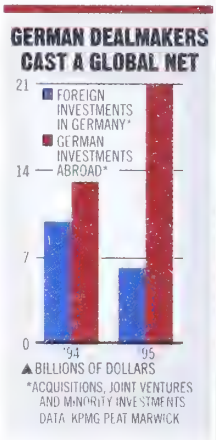
All of this, says Smith, suggests that sensitive-materials prices have been distorting the index of leading indicators. "Given the deepening gloom in financial markets," he says, "the optimistic picture painted by the index without sensitive materials is mind-boggling. The economy may have a lot more latent strength than many people believe."

ALL THE WORLD'S AN M&A STAGE

The U.S. dominates the action

The pace of cross-border mergers and acquisitions hardly slackened last year, reports KPMG Peat Marwick, as the value of global deals surged 17%, to $229 billion, and the number of $1 billion-plus deals jumped to 48 from 37 in 1994.

As usual, U.S. companies led the pack in both purchases and sales—raising its investment outlays by 46% to $64 billion while attracting $60 billion from foreign companies seeking to establish or widen their bases in America. The biggest increases among investment targets were posted by Britain, Australia, and Russia, whose deals rose by $20 billion, $10 billion and $8 billion respectively. Spending for deals in China and Germany, by contrast, fell by $7.2 billion and $3.7 billion.



Indeed, with its foreign purchases rising 61% and sales to foreigners falling 38%, Germany wound up as 1995's largest net exporter of deal capital. Spurred by the strong mark and domestic economic woes, German companies are increasingly keen to expand their operations in foreign markets.

DOES WELFARE ACT AS A MAGNET?

Not enough to spur migration

Critics of current U.S. welfare reform plans, which would give states a lot more flexibility in setting benefit levels, charge that such changes would touch off a "race to the bottom." That is, states with relatively high benefits would either have to match the cuts made in other states or face the possibility of an influx of welfare recipients looking for the best deal.

But do welfare recipients actually migrate across state lines in search of more generous benefits? Not in significant numbers, says a new National Bureau of Economic Research study by Philip B. Levine and David J. Zimmerman. Using survey data from 1979 through 1992, the two economists compared the interstate migration of poor single women with children eligible for welfare (Aid to Families with Dependent Children) to moves by poor people ineligible for welfare such as single men, childless women, and married couples.

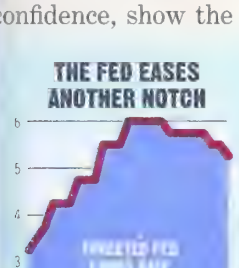
The study turned up scant evidence of welfare-induced migration. Poor women eligible for welfare were no more likely to move from a low-benefit state to a high-benefit state than similar poor people ineligible for welfare.

BY JAMES C. COOPER & KATHLEEN MADIGAN

THE FED WILL COAX CONSUMERS OUT OF HIBERNATION

U.S. ECONOMY Basketball superstar Magic Johnson may not be the only comeback story for 1996. After a winter respite, U.S. consumers will get back into the game, too. But don't expect too much.

Households are a little out of shape, and their eventual return to the malls is likely to look far less impressive than Magic's reappearance on the hardwood. Consumers are carrying around an increasing amount of debt in a job market that is a lot softer than it was a year ago. Incomes are not growing as fast, either, and rising loan delinquencies, along with the downbeat tone of both December retail sales and January consumer confidence, show the strain.



But consumers are not ready to bow out of this five-year-old expansion. Jobs and incomes may be sluggish, but they are growing. Joblessness remains low, and worries over consumer debt are exaggerated, especially with lower interest rates to ease the burden.

The Federal Reserve cut its target rate on overnight borrowing between banks by a quarter-point on Jan. 31, to 5.25%, following a similar reduction at the Fed's previous meeting six weeks earlier. The federal funds rate is now three-quarters of a point lower than it was last July (chart). The Fed also cut its discount rate to 5%, from 5.25%, and commercial banks trimmed their prime rates from 8.5% to 8.25%.

The Fed said that "moderating economic expansion in recent months has reduced potential inflationary pressures going forward." That statement, following back-to-back cuts, shows that the Fed is increasingly attentive to the economy's recent signs of softness, and another cut this spring appears likely.

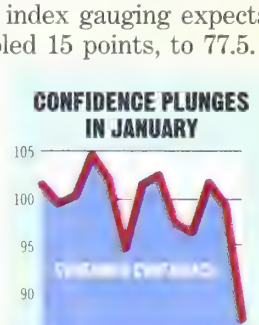
THAT'S BECAUSE policy still looks tight, in light of such a benign inflation outlook. Although a weather-related spike in energy prices caused a 0.5% increase in the producer price index of finished goods in December, the core index was up only 0.1%. With consumer inflation running at about 2.5%, a federal funds rate of 5.5% meant that real rates were as high in January as they were at the peak of Fed tightening a year ago.

Whether intentional or not, the timing of the latest rate cut is particularly fortuitous for Federal Reserve Chairman Alan Greenspan. He is facing renomination, not to mention his semiannual testimony on the conduct of monetary policy on Capitol Hill on Feb. 20.

Staring at fall elections, Congressional members are likely to grill the Chairman on why households appear so despondent. Consumer confidence, as measured by the Conference Board's index, plunged 12 points last month, to 87, the lowest reading in nearly two years and the biggest one-month dip in four years (chart). The board says it remains to be seen whether the drop is just temporary or signals slower growth.

For now, it looks as if it's the former. Consumers were buffeted in January by high-profile layoff announcements at AT&T and Apple Computer Inc., a second shutdown of the federal government, and loose talk about a default by the U.S. Treasury—all while Mother Nature was dumping two feet of snow on most of the East Coast. That's enough to sour anyone's spirits.

The trouble is, consumers will not plunk down money, especially for big-ticket items such as cars and houses, unless they feel good about the future. While the index reflecting households' view of present conditions fell 8 points, to 101.3, the index gauging expectations of future conditions tumbled 15 points, to 77.5.



Consumers are already holding back on buying cars and homes, despite lower rates. January car sales appear to have fallen back after sales promotions inflated the December results. And sales of existing homes fell 3.2% in December, the third decline in a row.

But while the recent lethargy in consumer buying is likely to persist through the winter, it doesn't signal a deterioration in consumer fundamentals that could plunge the economy into recession.

For all the ink spilled over the "disastrous" holiday shopping season, December retail sales still posted at least a tepid 0.3% gain on the heels of November's 0.7% advance. And early reports from department and chain stores for January show some improvement.

THE RETAIL SALES NUMBERS bear out the publicized notion that traditional department store sales got hammered last quarter, though sales elsewhere fared somewhat better. Retail sales in the fourth quarter rose at a lackluster annual rate of 1.9% from the third quarter, the smallest increase in four years.

However, that weakness partly reflected a 4.3% dive

JEFF HOFFMANN-BW

in sales at department and other general merchandise stores (chart). That kind of drop has not been seen since the 1980 recession, when the sudden imposition of credit controls caused an 8.4% quarterly plunge in real gross domestic product. In fact, growth in total retail sales would have been one percentage point stronger if not for the general merchandise segment, which is only 12% of receipts.

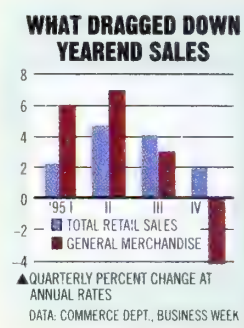
Car sales managed a solid 0.7% increase in December, but the dealers of Big Three carmakers still went into January with a glut of unsold cars totaling an 83-day supply, far above the preferred 60-day total. That means auto industry efforts to cut stock levels will be a big drag on industrial output early in 1996.

The blizzard will be another dead weight on reported output, as well as on other government numbers ranging from retail sales to employment to housing. Based on the data, January is bound to look like a disaster, which is sure to fuel talk of a consumer-led recession. Separating the wheat from the chaff will not be easy.

ONE THING THAT IS CLEAR, though, is that consumer finances, while hardly strong, are a long way from the sorry state that could precipitate a major pullback in spending. To begin with, the share of aftertax income taken by interest and principal payments on mortgage and consumer debt, while up in the past year, is well below its late-1980s peak.

Given the proliferation of floating-rate debt in recent years, the Fed's cuts in short-term interest rates are helping to lighten the monthly burden of servicing that debt. And because of lower long-term rates, many homeowners are refinancing their mortgages.

Moreover, while delinquency rates are rising, especially for bank credit cards, such tardiness is still low in most cases. The Fed's latest survey of senior loan officers shows no sign that banks are tightening credit standards. And financial market gains have strengthened consumer balance sheets to the point where financial assets are rising nearly twice as fast as liabilities. Unless the labor markets suddenly dry up—for reasons other than the weather—consumers seem likely to hit the malls again this spring.



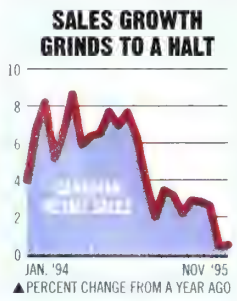
Don't expect a buying spree, though. With consumer spending growing at an annual rate of only 2.7% since early 1991, this is one of the weakest consumer expansions in the postwar period. But given that household spending is two-thirds of this economy, even a modest comeback by such an important player will undoubtedly make a significant impact on the game.

CANADA

EVEN WITH EASING, LOTS OF UNEASE

Canada's balancing act continues: On one side, a weak economy with chronic high joblessness. On the other, the need to rein in massive government debt and hold the Canadian dollar at levels where foreign capital will keep flowing in.

In an effort to keep this high-wire act from tumbling, the Bank of Canada cut interest rates by a quarter-point on both Jan. 25 and Jan. 31, surprising most analysts and suggesting that the BOC is uneasy about the economy's prospects. The second cut came only minutes after a U.S. rate cut. Private forecasters are increasingly pessimistic. The Royal Bank of Canada sees 1996 growth at just 1.8%, too slow to make a dent in the 9.4% jobless rate or to generate the faster income growth needed to jump-start consumers.



Consumer spending, in one of its worst slumps on record, has been held back by severe fiscal restraint, heavy debts, and uncertainty over Quebec sovereignty. Interest-rate cuts totaling 3 points since last May have eased the debt burden somewhat, as the yearend strength in housing starts and auto sales shows. Wage growth remains weak and continues to lag behind inflation.

Inflation finished the year at only 1.7%, below the midpoint of the BOC's target range, giving the central bank cover for its latest rate cuts. But because of the weak economy and narrowing yield spreads vs. the U.S., the rate cuts further depressed the Canadian dollar. At about 72.8¢ U.S., it is trading at levels well below those expected after the failed sovereignty referendum. And new polls suggest Quebeckers will vote *oui* when the issue comes up again—possibly before the end of 1997.

Until then, the economy's biggest drag is from federal and provincial budget cuts. Canada has made strides in correcting its fiscal imbalances and regaining investor confidence. And the government plans to trim the deficit to 2% of gross domestic product in fiscal 1997-98. Ontario, with its 40% of GDP, is considering tax cuts to help lift household incomes. But for this year, interest-rate cuts will be about the only relief for beleaguered Canadian consumers.

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THE ECONOMY

IS BUSINESS RUNNING SCARED?

A retreat from capital spending may worsen the slowdown

What a performer. While other sectors of the U.S. economy stagnated last year, Corporate America laid out big bucks for new computers, industrial machinery, and other productivity-enhancing equipment. The splurge provided the economy with its backbone: A stunning 56% of economic growth during the first nine months of 1995 came from higher capital spending (chart).

Now, free-spending companies are facing a further weakening economy—even in the face of the Federal Reserve Board's quarter-point rate cut on Jan. 31. Retail sales are lagging, and the Conference Board's index of consumer confidence plummeted to 87 in January from 99 a month earlier. Key export markets such as Japan and Germany are still slumping. And factories are running at only 82% of capacity, down from 85% a year ago.

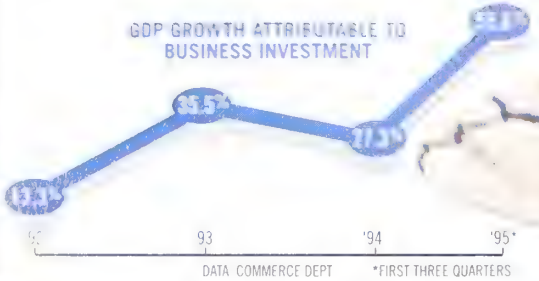
In the face of all that, many companies report they're planning small or no investment increases in 1996 vs. 1995, while others are actually cutting capital budgets. Production of business equipment is growing at only 3.6% annually, down from triple that growth rate at the beginning of 1995. "For the first time [in this cycle], the slowdown in the economy is dragging down the extraordinary growth in capital spending," says Jerry J. Jasinowski, president of the National Association of Manufacturers.

SHAKY DISCIPLINE. The danger is that a hasty retreat from business investment in 1996 could turn a slowdown into a recession by removing a key support for economic growth. It has happened before. A decline in capital spending in late 1989 and early 1990 laid the groundwork for the 1990-91 recession. A similar decline could also make it harder for the U.S. to generate higher productivity growth over the long run.

Corporate executives swore they wouldn't repeat the pattern this time. Throughout this expansion, they have talked about investing to meet long-term goals of cost-cutting and creating new products, rather than responding to the gyrations of the business cycle. If companies stick to the plan, capital spending, adjusted for inflation, could grow 4.7% in 1996, estimates Laurence H. Meyer & Associates, an economic forecasting firm. That's down from the 7.5% rate of 1995, but it's still strong.

The promise of long-term investment discipline, though, is untested at best. Already, there are signs that business, anticipating a sluggish economy, is throttling back. Tennant Co., a $320 million maker of industrial-floor maintenance equipment, had hoped to boost capital investment in 1996 by 5% to 10%. Now, "we're taking another look at our plans and will be slowing down a bit," says Chief Executive Officer Roger L. Hale. More ominously, DuPont Co. Chief Financial Officer Charles L. Henry

CAPITAL SPENDING KEPT THE ECONOMY



says: "We might not increase [capital spending] at all from where we were in 1995 f business is not better."

The semiconductor industry could be among the most sensitive to an economic slowdown. With billions of dollars of new chip factories in the works, there could be a major glut if demand drops.

Given the rising share of PCs going into the home, the semiconductor industry may be getting "much more wired into the macro economy," says G. Dan Hutcheson, president of VLSI Research in San Jose. "If the economy goes into the tank, the industry will go with it."

Among computer makers, Compaq Computer Corp. is upbeat about 1996 sales, and plans to boost investment by almost 11%. However, there's no major bricks-and-mortar construction that cannot be deferred if its present optimism sours. "Because [most of] what we're doing is modifying current structures and adding equipment, we are flexible," says Compaq CFO Daryl J. White.

Some companies, still digesting their large 1995 investments, may be quite willing to cut back in 1996. Southern Pacific Railroad Corp., for one, spent $900 million on capital equipment last year, including 279 locomotives, the largest single order in railroad-industry history. In 1996, SP will bring spending down to $350 million. Haggar Corp., the Dallas-based marketer of men's wear, spent $31 million in 1995, much of it on a customer service center near Fort Worth. This year, says CFO Ralph A. Beattie, Haggar will shell out about $6 million. Purchasers of heavy-duty trucks may be satiated as well: After a record-breaking 1995, North American production of heavy-duty trucks will decline about 20% this year, says Adrian T. Dillon, chief financial and planning officer of Eaton Corp., a large supplier of truck parts.

Certainly the U.S. airline industry is being cautious. AMR Corp., parent of American Airlines Inc., has repeatedly said it won't buy new planes until it can lower its labor costs and get a better return on investment. As a result, AMR's capital spending will be down about 3% this year. And Continental, which just reported its highest quarterly profits ever, has deferred its orders from Boeing Co. from '96-'97 to '98-'99.

SHORT-TERM FEARS. Even when U.S. companies do boost capital spending, much of the new investment will go overseas. GE Capital Aircraft Leasing, which recently ordered $4 billion in planes from Boeing, expects most customers to come from Asia. General Motors Corp., too, is looking abroad. "We expect U.S. capital spending to stay about the same," says J. Michael Losh, CFO at GM. "The growth in capital spending is overseas." GM is investing $1 billion in a new carmaking venture in Shanghai.

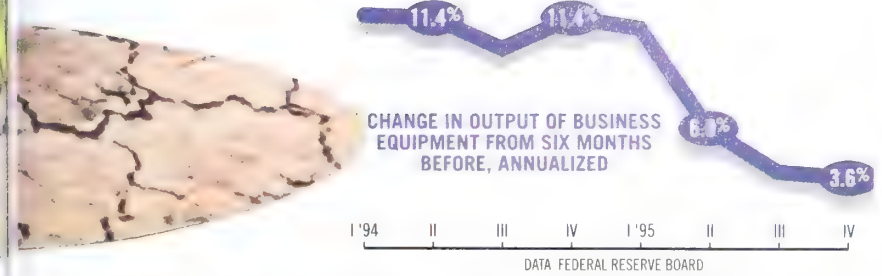
Where does capital spending remain strong? Despite falling capacity utilization, companies are still building new factories. Eaton, for example, is adding new facilities after years of packing more equipment into the same factory space. "We've crammed as much as we can" into existing buildings, says Dillon. Capital investment may stay strong in industries like steel, where factories are still running at full tilt. "We're busy, everyone's busy," says Dom DeSalvo, president of D&L Inc., a builder of steel mills that is erecting a big new plant for Nucor Corp. in Charlotte, N.C.

And Molex Inc. isn't backing off. The $1.2 billion maker of connectors and switches set a $200 million investment budget last summer. But rather than reduce its capital spending when conditions changed, Molex is shifting from slow-growing markets like appliances to automotive electronics and telecommunications, where growth remains strong.

The willingness of companies like Molex to keep investing, even if the economy stalls, will help determine whether the U.S. suffers a mild downturn or a head-on recession. We'll see whether U.S. businesses have really developed the long-term vision and discipline needed to compete in the world economy—or whether their short-term fears ultimately will win out.

By Michael J. Mandel in New York, with Zachary Schiller in Cleveland, Stephanie Anderson Forest in Dallas, and bureau reports

)WING, BUT NOW IT'S SLOWING TO A TRICKLE

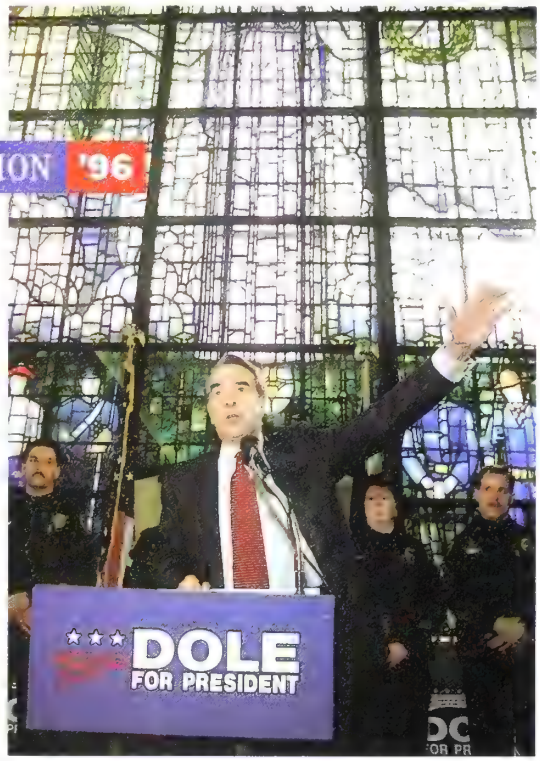


THE GOP

SENATOR DOLE, YOU'RE SWEATING

How the GOP front-runner is scrambling to reverse his slide

As political events go, Bob Dole's Jan. 24 visit with cops in Cedar Rapids, Iowa, wasn't a barn burner. First, Police Chief Bud Byrne lauded a White House-backed program that helped him hire five new cops—a bill Dole opposed. Then came the moment photographers adore and politicians dread: trying on the funny hat. "Is it the right size?" Dole groused as he awkwardly donned a baseball cap. "How bad is it?"



ATTACKING The senator, at a war memorial in Cedar Rapids, is starting to blast Forbes, known in the Dole camp as "the geek"

Pretty bad, senator. As early GOP contests loom in Iowa and New Hampshire amid rising unhappiness with the Presidential field, the Senate Majority Leader is discovering just how perilous the life of a front-runner can be. Dole's problems exploded on Jan. 23, when he gave a wobbly and wooden response to President Clinton's well-received State of the Union speech. Then came a spate of polls showing that millionaire publisher Steve Forbes was vaulting out of the pack (charts). Although Dole strategists privately scorn Forbes as "the geek," Forbes's charge has created a crisis of confidence in a politician who once seemed poised to capture the nomination without breaking a sweat.

"I'm not even sure I'm voting for myself," Dole wisecracked during his Iowa swing. Nobody on the Kansan's campaign team, though, is laughing. Dole placed a weak third in Alaska's Jan. 27-29 straw poll behind commentator Patrick J. Buchanan and the free-spending Forbes. Then, in a special election on Jan. 30, Oregon voters turned a GOP Senate seat over to Democrat Ron Wyden, suggesting a hard fight ahead against President Clinton. "Dole is not the leader America needs right now," frets Gary W. Baker, 62, a Rochester (N.H.) school administrator, who nonetheless leans toward Dole. "He doesn't seem to give people hope."

Maybe not, but he does have some striking advantages over rivals: solid grassroots organization, massive recognition, and loads of big-name endorsements. Dole also has a comeback plan. Key elements of his survival strategy:

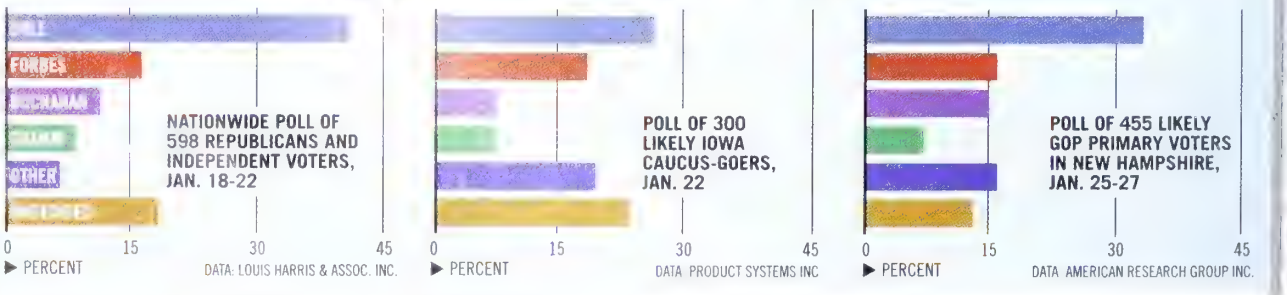
■ **Hit back.** Dole believes his '88 campaign made a fatal mistake by not responding to George Bush's attack ads in New Hampshire. He won't lay back again. After Forbes whomped him for favoring tax increases and congressional perks and pay raises, he took to the airwaves to decry Forbes for "untested leadership" and "risky ideas."

■ **Play up populist themes.** In coming days, Dole will contrast his hardscrabble roots with Forbes' silver-spoon upbringing. At a recent rally in Clinton, Iowa, Dole pointedly mentioned that his parents scraped by on welfare during the Depression. Aides happily remind voters that Forbes's *père*, on the other hand, owned a yacht, a French chateau, and a jet called the Capitalist Tool. Dole claims Forbes's flat tax would "shift the tax burden from the superrich to middle-class Americans.... Those of you with a helicopter pad on your yacht, grab it."

Dole's people view Forbes as the only current threat for the nomination. "Ultimately, Dole has to take Forbes apart as a rich guy who's trying to buy an election," says one adviser. Forbes partisans say the attacks will only reinforce doubts about Dole. "He'll just get meaner, and that will hurt Dole," says Forbes pollster John McLaughlin.

■ **SOS to Christian conservatives.** Religious activists are nervous about Forbes, who has supported abortion rights and gays in the military. But their loyalties are split among Dole, Buchanan, Texas Senator Phil Gramm, and conservative activist Alan L. Keyes. Dole hopes the Forbes threat solidifies

AS THE PRIMARIES BEGIN, DOLE IS UNDER FIRE



religious activists, who hold the balance of power in early battlegrounds such as South Carolina and Florida. The gambit may be working: On Jan. 25, Phyllis S. Schlafly, chairman of the Republican National Coalition for Life, pronounced "artful dodger" Forbes unacceptable.

Dole is hoping to reverse his slide before the Feb. 12 Iowa caucuses. But he's still slipping. A Jan. 22 poll found that Dole's support had dipped from 36% to 26% since November, while Forbes's backing grew from 8% to 18%. The situation in New Hampshire is even more volatile, according to two polls released Jan. 29. An American Research Group Inc. survey of likely GOP primary voters found Dole leading Forbes 33% to 16%. A poll by the Pew Research Center for the People & the Press showed Dole narrowly ahead of Forbes among Republicans. But independents favor Forbes by a 2-to-1 margin.

Despite his troubles, Dole is still favored to win Iowa. The key battle is for second place. Gramm has a deep organization, but Forbes—unburdened by spending limits—is investing some $3 million in hopes of an upset. Will spending alone do the trick? Dole and Gramm are organized in all 99 counties, but Forbes has just 34 county coordinators.

DOLE'S MAGINOT LINE. The second-place finisher in Iowa will get a strong push in the New Hampshire primary eight days later. A key moment there could come in the state's big Feb. 15 debate, a forum that has provided aspiring candidates, including Ronald Reagan in 1980, a chance to break from the pack.

If Dole stumbles in New Hampshire's Feb. 20 primary, his first line of defense comes on Mar. 2 in South Carolina, followed by New York on Mar. 7. The last bastion in Dole's Maginot line: the Mar. 19 Midwestern primary, where three popular GOP governors are going all out for the Kansan.

Still, Dole will need more than endorsements to win the nomination in an era when politicians of all stripes are suspect. Ultimately, he must win over voters such as Byron Shaw of West Burlington, Iowa: "I respect Senator Dole," the Vietnam vet says. "But he just doesn't come across as a leader to provide change." Adds Forbes backer Ryan Miller, an Iowa City chiropractor: "People are looking for something other than a career politician."

Such sentiments could be fatal. Dole's hope for regaining his equilibrium is to silence the doubters—and squash Forbes—before the pre-primary jitters turn into open rebellion.

By Richard S. Dunham in Cedar Rapids, Iowa, with Susan B. Garland in Nashua, N.H.

DICK ARMEY: IMMOVABLE FORCE OR SITTING DUCK?

For partisans of both parties, it was an exquisite moment: former House Republican Leader Robert H. Michel, a model of GOP consensus-building and conciliation, wagging his finger at fiery ideologue Richard K. Armey, the current House Majority Leader. "The Republican Party is through . . . because of you," Michel scolded.

The audience at Washington's Arena Stage burst into applause. The two veteran pols were merely reciting lines in a Jan. 29 benefit performance of the stage classic *The Front Page*. But Armey also is giving quite a performance as House floor leader. His hard-line stands are delighting staunch conservatives, and they're elating Democrats, who hope to paint Armey as an extremist in political campaigns this fall.

NO QUARTER The blunt Texan thrills staunch conservatives, but Democrats think they've found a target

ROILING MARKETS. Armey's recent prominence has coincided with House Speaker Newt Gingrich's decision to step back a bit, amid sagging polls and a House ethics committee probe. Armey also has been boosted by House GOP freshmen and conservative activists, who demanded that he join the Speaker at White House budget negotiations. They view Armey as more distrustful of President Clinton's motives and less impulsive than Gingrich. "In fashioning compromise, Dick will never sacrifice conservative values," says Texas Republican Party Chairman Tom Pauken.

Armey's blunt style is making waves far beyond the Beltway. On Jan. 21, he rattled the financial markets when he said on NBC's *Meet the Press* that Republicans might use the threat of an unprecedented U.S. government default to win concessions from President Clinton. His comments marked an about-face from the conciliatory GOP rhetoric of preceding days. "Disturbing," said White House Chief of Staff Leon E. Panetta. Federal Reserve Chairman Alan Greenspan went to Capitol Hill to lecture Armey about the danger of spooking investors.

"THE GRIM REAPER." Armey is used to controversy. Since he was first elected in 1984, the 55-year-old former University of North Texas economics professor has happily taken the heat for his crusades against federal spending. He has even tackled such GOP sacred cows as military bases and farm subsidies. "I am—and have been in the years I've been here—more conservative than Newt," he brags.

Armey admits that his blunt style doesn't always help his cause. "I don't have the skill to be guileful," he says. "If you catch me in the backyard or on national TV, I'll tell you the same thing." Even one prominent Republican senator privately refers to him as "the grim reaper"—death to all government programs, even GOP favorites.

That's an image that Democrats want to promote. They see Armey as a frightening face of GOP extremism that they can exploit for political benefit. "He's the embodiment of the Republican Revolution," says Representative Barney Frank (D-Mass.). "He's now part of the campaign for every Democrat running for the House."

Armey's current agenda is sure to keep Democrats baying. On top of pushing his pet project, a flat income tax, he plans to champion further deregulation, doing away with the Commerce Dept., and more curbs on abortion. Will it play politically? Voters will determine that in November if they maintain the GOP majority—and give Armey an encore.

By Richard S. Dunham, with Mike McNamee in Washington

SPIN-OFFS

TENNECO MAY HAVE TO GET SMALLER TO GET STRONGER

Disappointing earnings pump up the pressure to sell divisions

For almost four years, Tenneco Inc. Chief Executive Dana G. Mead relied on patient investors while he reshaped the big conglomerate around a handful of businesses. In everything from paper boxes to shipbuilding, Mead has tried to refocus Tenneco on growth markets for consumer packaging, international power, and auto parts—spending $2.3 billion on acquisitions in the past 18 months to help whip operations into shape.

Now, a further breakup may be inevitable. Mead, 59, is still fighting to complete his turnaround, but pressures are building for a quick spin-off of one or more divisions. The most likely first candidate: its huge shipbuilding operation in Newport News, Va., which analysts value at $1.2 billion (table). Mead says no decision has been made on Newport News. And he says he isn't planning a full breakup of the company, though he might do one in the future. But some sort of spin-off seems likely. Citing past public offerings of its Case Corp. and Albright & Wilson Inc. subsidiaries, Mead says: "You can count on further strategic action soon." Tenneco shares jumped more than three points on Mead's Jan. 30 hints to analysts of some sort of sale, closing at 51⅞ on Jan. 31.

Why move now? On Jan. 30, Tenneco reported 1995 operating earnings of $1.3 billion on sales of $8.9 billion, below Wall Street projections and a sign that further gains will be harder to come by. The lone division to increase operating income in 1995, Tenneco's $2.8 billion packaging unit, faces margin pressure this year from falling linerboard prices and an accelerating industry consolidation. Net income did rise 80%, to $735 million—a striking revival, compared with a $1.3 billion loss three years ago—but the results haven't translated into a big stock rise. Indeed, in October, the Council of

WHAT'S TENNECO WORTH?

	BILLIONS
TENNECO ENERGY	$2.8
TENNECO AUTOMOTIVE	2.2
TENNECO PACKAGING	2.9
NEWPORT NEWS SHIPBUILDING	1.2
CASE	0.7
TOTAL	$9.8
SHARES OUTSTANDING	170.6
PER SHARE VALUE	$57.50

DATA: PAINEWEBBER INC

MEAD AND STOCK ANALYSTS IN '93: *Wall Street still isn't happy*

Institutional Investors put Tenneco on its list of stock underperformers. One reason: Last year, its shares (including dividends) rose just 20.8%, vs. 37.5% for the Standard & Poor's 500-stock index.

Mead wants to do better. "We're determined to build value" by investing in new markets and higher-margin products, he says. He pledges to chop $200 million from working capital this year, freeing up cash for stock buybacks and operations. By pooling Tenneco divisions' purchasing of professional services, maintenance, and supplies, Mead plans to wring an additional $100 million annually out of operating costs starting in 1997—on top of a $30 million cut last year.

SHOCKS AND MUFFLERS. The cash from selling 79% of Case has gone into acquisitions—such as the November purchase of Mobil Oil Corp.'s plastics operation. That alone should add $1.3 billion to 1996 revenues and contribute more than $100 million in operating profits, say analysts. Elsewhere, Mead is arranging joint ventures in expanding auto markets such as China and India—and scouring the globe for acquisitions to beef up sales of auto shock absorbers and mufflers. A breakup now, Mead cautions, would not reward investors sufficiently: "Our assessment is there isn't a lot of extra value" in doing so at this point, he says.

But Tenneco's turnaround could get sticky. Mead must not only replace the $110 million in earnings from Case, whose earnings will be deconsolidated this year, but also smoothly integrate its 18 recent acquisitions. Meanwhile, its energy division's expansions into gas marketing and international pipelines haven't panned out. The biggest growth prospect, a $700 million pipeline from Argentina to Chile, faces fierce competition from a rival consortium. Some analysts, including PaineWebber Inc.'s Ronald J. Barone, think a Tenneco breakup is inevitable: "They have put up fantastic numbers, and the market has not rewarded them for those numbers," he says. He figures Tenneco is worth some $57.50 per share, plus $11 to $12 in breakup premium.

A huge payoff isn't certain. Shares of Hanson PLC, the British conglomerate, jumped but then fell again after it announced on Jan. 30 that it plans to split itself apart. But shareholders of AT&T and ITT Corp., among others, have seen big moves in their stocks on news of breakups. The lure of such lucre might prove too much for Mead to ignore.

By Gary McWilliams in Houston

HOW MUCH FOR ONE APPLE, SLIGHTLY BRUISED?

Analysts say Sun's lowball bid is close to the mark

Who to believe? In mid-January, Apple Computer Inc. insiders were whispering that Sun Microsystems Inc. had offered $33 a share for the troubled computer maker. Sun sources insisted their offer actually was closer to the mid-$20s. Now, the talks are stalled over—you got it—price. So what is Apple really worth?

Shockingly little. Attaching value to a company in flux is always tricky. But experts say Sun's lowball price is closer to the mark than the $33 Apple is still hoping for. PaineWebber Inc. analyst Michael K. Kwatinetz pegs the current value of Apple shares at $28, just above where the stock settled on Jan. 31 on rumors that talks with Sun had finally fizzled.

NO PREMIUM. Unfortunately for investors, that's Apple's 18-month low, and just $4 above book value. The reason: Apple's stock has lost the premium it used to command for its sterling brand name, 20 million die-hard customers, and products that were uniquely easy to use. Analysts differ over what Apple's various parts are worth, but most come to a similar conclusion. "The value of Apple's brand and customer base is declining at an accelerating pace," says CS First Boston's C. William Gurley.

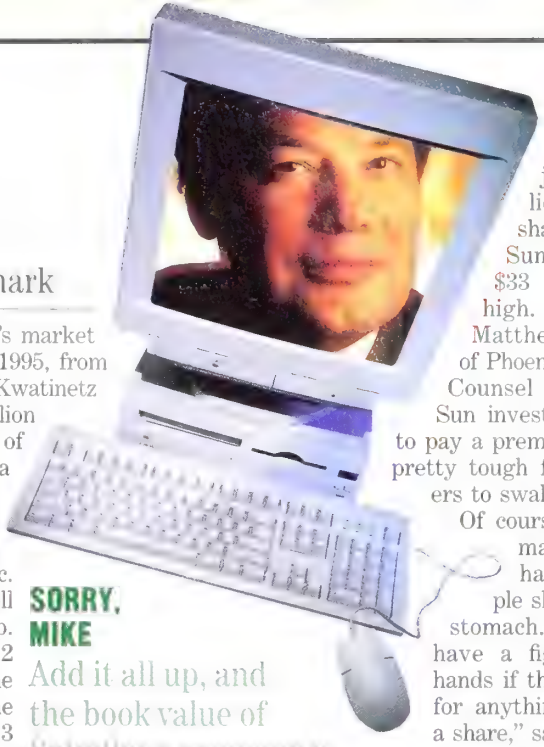
An analysis of Apple's breakup value reflects the devaluation. Take the company's marquee Macintosh operating system, one of its five core businesses. While Apple doesn't break out sales or profits for the Mac operating system, Kwatinetz figures the company gets some $55 per copy. That's more than Microsoft Corp.'s average of $49 per copy of Windows, though a far cry from the $375 Apple got in 1992.

At $55 a copy, Apple can expect $323 million in 1996 operating-system revenue. But that's below the $400 million it takes to maintain and market the software, says Kwatinetz. That's why he values the unit at just two times sales vs. Microsoft's six times sales. Apple's crown jewel is worth only $646 million.

So goes Apple's mainstay hardware business. With a disastrous Christmas helping to lower the Mac's market share to 7.8% in 1995, from 8.3% a year ago, Kwatinetz values the $11 billion unit at just 20% of 1996 revenues—a multiple somewhere between that of struggling AST Research Inc. and of steady Dell Computer Corp. That puts a $2.2 billion value on the Mac business—the industry's No. 3 player.

The same dismal picture applies to Apple's $1 billion printer business. The products are state of the art, but they work only with Macs, and printers are a low-margin business. PaineWebber figures the unit's value is some 20% of revenues—just $200 million. Apple's other hardware businesses—Newton, its handheld communicator, and Pippin, a multimedia game player that will debut this March in Japan—add perhaps $150 million more.

The picture brightens slightly at Apple's applications-software subsidiary, Claris Corp. Sales there should grow a healthy 50% in 1996, to $250 million. But since almost all of its sales are for the Mac, Claris doesn't command a premium. Value: $250 million.



SORRY, MIKE

Add it all up, and the book value of Spindler's company is a mere $3.44 billion. Why so little? Shrinking market share, for one thing

Add it up, and this $12.7 billion company is worth just $3.44 billion, or $28 a share. Suddenly, Sun's rumored $33 bid sounds high. Says analyst Matthew Considine of Phoenix Investment Counsel Inc., a large Sun investor: "For Sun to pay a premium would be pretty tough for shareholders to swallow."

Of course, a fire sale may be even harder for Apple shareholders to stomach. "Apple will have a fight on their hands if they try to sell for anything under $40 a share," says Jerome L. Dodson, president of the Parnassus Fund, which holds 340,000 Apple shares bought at an average price of $37.

One solution: Apple CEO Michael Spindler could slash costs, return Apple to profitability, then pursue a merger. The first phase of his restructuring, unveiled in January, calls for 1,300 layoffs and a streamlining of products—moves that will reduce expenses 10%. That's only half of what's needed, analysts say. Spindler is expected to order a new round of cuts by mid-February. Should he slash expenses from 19% of sales to 11%—Compaq Computer Corp.'s level—Apple could command a $40-plus stock price by 1997, says Vidim Zlotnikov, a Sanford C. Bernstein analyst.

The picture could get even better should Spindler focus on core markets, such as education and publishing, where he can raise prices without losing customers. That could drive the value of the Mac hardware unit to $4.4 billion. With aggressive licensing of the Mac operating system, the business could be worth $1.6 billion. Figure a slight uptick in the remaining units' values, and Apple's total value, says Kwatinetz, could be $7.1 billion, or $58 a share—double today's worth.

For Apple shareholders, that sounds too good to be true. It probably is.

By Peter Burrows, with Kathy Rebello and Robert D. Hof, in San Francisco

SLICES OF THE APPLE *An analysis of the computer maker's breakup value*

	1996 SALES* BILLIONS	MULTIPLE**	VALUATION BILLIONS
COMPUTER HARDWARE	$11.0	0.2	$2.20
OPERATING SYSTEMS	0.32	2.0	0.64
CLARIS SOFTWARE	0.25	1.0	0.25
PRINTERS, SCANNERS	1.0	0.2	0.20
NEWTON, OTHER	0.03	5.0	0.15
TOTAL	12.72	0.27	3.44
BREAKUP SHARE VALUE			$27.96
SHARE PRICE JAN. 31			$27.25

*Projected **Based on comparisons with poorly performing peers

DATA: PAINEWEBBER INC.

THE MARKETS

AS GOES JANUARY, SO MAY GO THE YEAR

Low rates, strong investor demand. The old adage might be true

After a rip-roaring 1995, many on Wall Street figured the bull market had to end—and soon. Well, the naysayers were wrong. On Jan. 30, the Dow Jones industrial average soared 74 points. The next day, it jumped another 14 points, to a new high of 5395. In all, the market posted a sizzling 5.4% gain in January, fueled by some surprisingly strong earnings reports, a Fed rate cut, and a flood of new money into equity mutual funds. And there's an old Wall Street axiom: As January goes, so goes the year.

Will it hold true? As recently as mid-January, the market didn't look so strong. Then, the Dow was down about 2% for the year. The Pacific Stock Exchange (PSE) Technology Index, which is full of high-tech stocks, fell almost 10% during the first 10 trading days of 1996. Disappointing earnings from companies such as Apple Computer Inc. and Motorola Inc. seemed to bode ill for the market generally.

TECH BOUNCE. As in 1995, though, the market is burying the pundits. The Dow aside, the PSE index now is up 2.3% on a solid bounceback in tech stocks. Stocks have been buoyed by the surprising pattern in fourth-quarter earnings reports, says William Quinn of I/B/E/S Inc. Normally, companies rush to get good earnings out early and delay announcing bad news. This year "we're seeing the opposite," says Quinn. Among relatively late reports of better-than-expected earnings: On Jan. 30, General Motors Corp. announced that fourth-quarter profits hit $1.9 billion, or $1.98 a share. That was up 19% from a year earlier and beat analysts' estimates by 67¢. The next day, Ford Motor Co. came in with quarterly earnings of $660 million, or 49¢ a share—more than double the 21¢ analysts had expected.

Is the optimism getting out of hand? Ben Zacks of Zacks Investment Research is cautious. He notes that GM benefited from an unusually low tax rate for the quarter. And Ford's profits were weak—net earnings fell 58% from 1994's fourth quarter—even though they beat expectations. Zacks credits the huge flow of money into the market with fueling most of the market's rise. Robert Adler, an analyst with AMG Data Services, notes that, as of Jan. 24, inflows into equity funds already had set a monthly record at $20 billion.

Still, there are plenty of fundamental reasons to expect the bull to keep running, including the Federal Reserve Board's quarter-point rate cut on Jan. 31. "At the same time that this new money is underpinning the market, you have a favorable monetary setting," says A. Marshall Acuff, portfolio strategist at Smith Barney Inc. "Interest rates could go even lower going forward, and that provides a strong sense of support for the market generally." Adds Anthony Dwyer of Josephthal, Lyon & Ross: "You have low inflation, which creates a lower interest-rate environment. That leads to a higher price that people are willing to pay for earnings."

Market folklore supports the bullish case. An analysis by Ibbotson Associates going back to 1926 shows that when the market had an above-average month in January—rising more than 0.8%—there was a 77% chance that it would have an above-average year. Pundits beware: So far, this market has a strong pulse.

By Suzanne Woolley in New York

AGRICULTURE

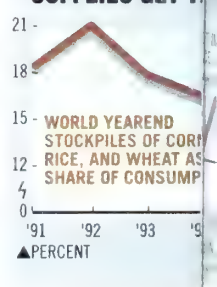
ASIA: FODDER FOR A CRISIS

Grain stockpiles dwindle in the face of surging demand

Kim Mee-Sook of Seoul knows how to make her two children happy: At least once a month, she puts away her rice bowls and heads to a steak house for Western-style sirloins. The Kims have company. Because of rising incomes, South Koreans, like many Asians, are eating twice as much red meat as in 1980.

A growing appetite for beef, pork, and poultry has triggered a surge in Asian demand for grain to feed livestock. China, once a top grain exporter, recently had to boost imports to meet its domestic needs (charts). And demand from Asia will only expand. "Asians are upgrading their diets and there are a lot of them, so the leverage is enormous," says James G. Kendrick, a University of Nebraska agricultural economist.

A crisis could be brewing, however. Poor harvests in the U.S., the former Soviet Union, South Africa, and Latin America have cut into world production. Global supplies of rice, wheat, corn, and other key commodities have dwindled to their lowest levels in years. That has sent prices soaring: U.S. corn prices are up from $2.11 a bushel in November, 1994, to $3.69 on Jan. 30, for in-



BEIJING BUTCHER: *Asia is eating more red meat*

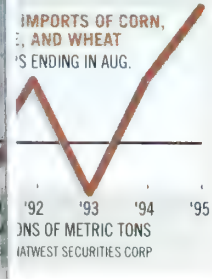
stance. The U. N. recently warned that food stockpiles stand far below the minimum needed "to safeguard world security."

Of course, fertilizer, pesticide, and seed companies stand to win from expanding production to fill the gap: IMC Global Inc. in Northbrook, Ill., expects Asia to account for more than half of its fertilizer exports this year, up from 35% a decade ago. And as the lowest-cost producers, U. S. farmers are well positioned to cash in. American agricultural exports are expected to jump to a record $58 billion this year, up 5% from 1991. But farmers worry that bad weather may cut into this year's crop. "There is no room for production problems," says Rockford (Ill.) farmer Jerry J. Gulke. "As it is, there are going to be some spot shortages."

PRICE FLUCTUATIONS. Most U. S. economists expect the surge in demand to have only a minimal impact this year on American grocery-store prices. Then again, meat prices could gyrate if the coming U. S. harvest is bad. Livestock producers have resisted reducing their herds in the hope that feed costs will raise. "They're all waiting for the other guy to blink," says NatWest Securities Corp. analyst David Nelson. If trouble sparks a sell-off, livestock prices would plunge as beef and pork flood the market, then skyrocket as supplies contract.

Beyond prices, a broader question looms: Does the world face a global food shortage, or can crop yields be increased? No problem, some experts say. China's production may well expand as the government steps up investment in farm mechanization. The U. S. government, too, is inviting farm expansion by eliminating a set-aside program that idled 7.5% of cropland last year. But urban encroachments have cut the world's harvested acreage by 8% from a 1980 peak. Even if farmers go all-out, it will take two or three bountiful harvests to refill the world's near-empty bins.

CHINA BUYS GRAIN



By Greg Burns in Chicago, with Joyce Barnathan in Hong Kong and Laxmi Nakarmi in Seoul

MARKETING

IS IT FINALLY MILLER TIME?

Its new flagship brand is aimed straight at Bud

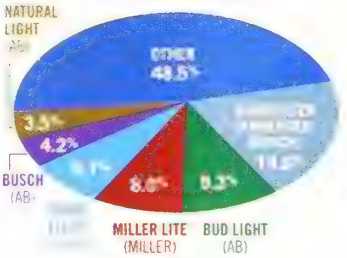
Nothing personal, insists John N. MacDonough. But ever since defecting in late 1992 from Anheuser-Busch Cos. to Miller Brewing Co., MacDonough has tried to outflank the No. 1 U. S. brewer. Now Miller's CEO, he came up with ice beer, introduced the Red Dog brand under the Plank Road Brewery logo, and is trying to parry every Anheuser thrust overseas with deals from China to South America.

TASTE TEST *Miller says that its new beer is fuller-bodied and less bitter than Bud*

Miller's U. S. market share—at 22.6%, a shade more than half of Anheuser's 44.2%—has barely budged. But 1995 operating profits, announced on Jan. 31, moved up a respectable 7.5%, to $446 million, on flat sales of $4.3 billion. Now, MacDonough is again sniping at Anheuser. Milwaukee-based Miller has just revamped its trademark, giving more prominent display to an eagle like Anheuser's. More significant: On Feb. 1, Miller is set to roll out a new flagship brand called "Miller Beer" that is intended to tarnish the crown of the King of Beers. MacDonough is confident the new brand, which he claims is fuller-flavored and less bitter than Bud, can take sales away from Bud, Coors, and others. "This tastes different from anything out there," promises MacDonough.

BEER WARS

1995 U.S. MARKET SHARE OF LEADING BRANDS



DATA: *BEER MARKETER'S INSIGHTS*

"WE'RE READY." Expect a battle royal. Miller plans to put some $65 million this year behind the new beer. MacDonough hopes the new offering will generate enough buzz to help Miller's three main brews, which are struggling. After an initial flurry of excitement, Miller's Genuine Draft has failed to gain broad geographic acceptance. Its market share is off slightly since 1993, to 3.4%. Onetime flagship Miller High Life has held its 2.5% share largely through price-cutting. And the once hot Lite brand, Miller's best-seller and the nation's No. 3 beer behind Bud and Bud Light (chart), eked out a small sales gain in '95 for the first time in five years. The new Miller brand, priced from $3.50 to $4 a six-pack, "is critically important to us," says Neil Harrison, Miller's marketing vice-president.

But Miller and other big brewers face a marketing dilemma. Beer sales have been flat for most of the '90s. Brewers have churned out an unprecedented array of new beers—ices, reds, ales, low-cal—trying to generate consumer interest but with virtually no effect on overall market share. Growth is coming from the low-calorie segment, now 40% of the market, and from scores of upstart microbrewers selling fuller-bodied, higher-priced beer. Bud has been hit especially hard: The market share of its main brew fell to 19.8% last year, off 1.8 points in two years.

Miller figures that middle-market consumers have developed a taste for a richer beer—at least, richer than Bud is perceived to be. One worry among some distributors is that the new offering may cannibalize current Miller brands. Still, they're enthusiastically toasting the new introduction. "I truly believe this is the best beer Miller has ever made, and we can grab some market share," says Kevin R. Burke, who owns Miller distributorships in the Chicago area, Louisville, and Oakland, Calif.

And what of Anheuser? Its beer earnings have been choppy through the '90s, including a flat 1995, estimates PaineWebber Inc.'s Emanuel Goldman. To boost Bud sales, Anheuser has retooled its advertising and sales force. It also is pushing its distributors to work aggressively with retailers and tavern owners to promote its brands over Miller's. "We're ready for [the new] Miller, and they'd better be careful to watch their backsides," says Robert C. Lachky, vice-president for the Budweiser brands. "We will be glad to take shelf space from Genuine Draft and Lite."

MacDonough, who commands wide respect from his former colleagues, almost seems to relish the skirmish. "Bud has left a position uncovered for a beer with more taste and drinkability," he contends. Beer drinkers will decide who wins the next round. Cheers.

By Richard A. Melcher in Chicago

TELEVISION

NIELSEN SCHMIELSEN

Now, the networks are calling the service a miserable failure

Not much bothers network television executives. Pampered stars, budget overruns, *Central Park West*—all this they can handle. But weekly ratings, they can send blood pressures up in a heartbeat. A point up or down, after all, can make or break a sitcom—and cost millions in lost ad revenue.

That is why Nielsen Media Research, which has monopolized program ratings since 1993, is in the TV industry's crosshairs. Executives at Fox Broadcasting Co. and NBC Inc. have blasted the 45-year-old TV rating operation for slipshod sampling and skewed results. Speaking to Fox affiliates in Las Vegas on Jan. 21, Fox TV Chairman Chase Carey called the service "unprofessional and unacceptable" and said he was contemplating legal action. A week later, NBC Television President Neil S. Braun openly wondered whether broadcasters should accelerate plans to

UNHAPPY TRAILS Does Nielsen underscount child viewers?

create a ratings service of their own.

The revolt coincides with Nielsen's expansion of its national survey, a move that broadcasters say overstates cable viewership by as much as 5%. "It's all about reliability and consistency," says Braun, "and in those areas, Nielsen is just not doing the job." In Green Bay, Wis., says Fox's Carey, Nielsen's numbers in November had ratings for *Beverly Hills 90210* dropping 86% from one week to the next. In Jackson, Miss., Fox says, a local affiliate posted ratings when it wasn't on the air. Network ecs say Nielsen chronically u counts demographically valu kids, who typically don't both record their viewing habits.

Nielsen acknowledges ther problems. "Anytime you deal sampling like this, you're goi get errors," says Vice-Presi Jack Loftus. The company special probes and telephone into sets in nearly 5,000 home tionwide. Yet it concedes tha til recently, only half of the domly selected families accep offer of the devices, skewin sults. Of those who do, few the buttons on the equipment to ind their age or sex.

In local markets, where advert is growing fastest, Nielsen's results be even more questionable. The com spreads just 300 to 400 meters a each of the nation's 33 biggest mar Those machines measure only w shows people watch; to get demog ics, Nielsen relies on diaries se 250,000 viewers, who are asked to in which programs they watch and w But Nielsen pays just $1 a week fo effort, so only half the diaries ar turned—and most of those are comp by adults, further distorting the re

PEOPLE

JIM MANZI'S SOFT LANDING

But can he adjust to the collegiality of Industry.Net?

Former Lotus Development Corp. CEO Jim P. Manzi, newly named CEO of Industry.Net in Pittsburgh, leans back in his swivel chair and nearly tumbles. He catches himself and leans back again, with the same result. Turns out his chair is missing a wheel. "That's an I.Q. test," quips the former classics scholar. "I'm still on probation."

In fact, the 44-year-old Manzi, who sold Lotus to IBM last year in a $3.5 billion deal that earned him $78 million, may have felt he was on probation at Big Blue. He lasted just three months as a senior vice-president before IBM's immensity and his relative lack of power got the best of him. With Industry.Net, he is clearly in charge, leading just 150 employees. Their mission: to pioneer all-electronic commerce with an online marketplace for a myriad of industrial goods. At Industry.Net, in which he is now a major investor, Manzi escapes the brutal packaged-software business, where he foresees only more "price destruction." Here, he's running an Internet company—the hottest area for initial public offerings—and he acknowledges that it may soon go public.

Public or private, Industry.Net faces plenty of challenges. Several E-commerce rivals have recently been launched. And Industry.Net must persuade corporations to use its services rather than set up shop on the Internet on their own. Plus, Manzi, known for having churned and burned top executives at Lotus, faces a cultural adjustment at Industry.Net, a collegial company that grew out of Carnegie Mellon University.

VALVE MAKERS. Founded six years ago by its chairman, Donald H. Jones, who still has close ties to CMU, Industry.Net has built a sizable business. Already, 3,500 manufacturers, from IBM, Honeywell, and Westinghouse to small valve and pump makers, advertise on its Web-based catalog. They pay $3,000 to $8,000 a year for listings that purchasing agents then browse online from their PCs. Industry.Net's take million last year, according to one mate. Growth rate: some 200% a ye far, according to the company. For no customers buy goods as usual, from distributors, but Jones says Industr will soon begin processing orders and ments, too.

What's Manzi's vision? First, tak dustry.Net abroad to link supplier customers across Europe and Asia. I he notes, raked in hefty profits t Plus, the sheer volume of business

BEYOND PITTSBURGH: *Manzi may take Industry global, but E-commerce rivals are moving in fa*

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HE UMP. That may not be enough
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Ronald Grover in Los Angeles, with
th Lesly and John A. Byrne in
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Industry.Net will generate lots of
e data. "These are new forms of in-
on," he says, "with plenty of down-
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ble is, Industry.Net's competitors
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n Manzi joined Industry.Net in late
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But who knows? Perhaps his se-
ecs, many of them fresh out of ac-
will gladly put up with some extra
e—if their new boss can convince
e'll make them a bundle, too.

Stephen Baker in Pittsburgh, with
. Verity in New York

LIGHTS! CAMERA! CHECKBOOK!

Edgar Bronfman is spending big on MCA. But on the right things?

After spending $5.7 billion for 80% of MCA Inc. last spring, Edgar Bronfman Jr. probably was expecting some flashy digs. Instead, the Seagram chief executive got the 16th-floor office once occupied by MCA founder Jules Stein. The wood-paneled shrine hadn't been touched since Stein's death in 1981, and the decor—a clutter of second-rate antiques and turn-of-the century horse paintings—was decidedly faded.

Bronfman has quickly overhauled the corner office—and almost everything else at MCA, moving aggressively to remake a company regarded for years as the stodgiest in Hollywood. MCA has lured the likes of Sylvester Stallone and Demi Moore to the studio for rich, long-term deals, and enticed a stable of heavyweight directors and producers. Insiders say it soon will spend $200 million to buy a half-interest in rap-music label Interscope Records. And in early February, Bronfman will announce a multibillion deal to build a theme park in Osaka, Japan.

SLY MOVES

Are Sylvester Stallone and Demi Moore worth the rich, long-term deals they cut with the studio?

FILL 'ER UP. It's a splashy entrance, for sure. "Edgar is certainly putting a lot of gas into the tank," says longtime friend David Geffen. But is it smart? Hollywood is less certain about that. It wasn't so long ago that Sony Corp. spent its way into a $3 billion write-down. Stallone, who last starred in the 1995 mega-dud *Judge Dredd*, is a big gamble at $20 million a film, and Moore, late of *The Scarlet Letter*, is no sure thing, either.

Bronfman does win kudos for remaking one of the oldest management teams in the business. He brought in as President Ron Meyer, former president of Creative Artists Agency Inc. It is Meyer who lured Stallone and Moore, both onetime clients, and signed Jim Carrey for $20 million to star in the film *Liar, Liar*. He also coaxed *Jurassic Park* director Steven Spielberg into doing a sequel, *The Lost World*, and re-signed *Apollo 13* director Ron Howard to a long-term contract extension.

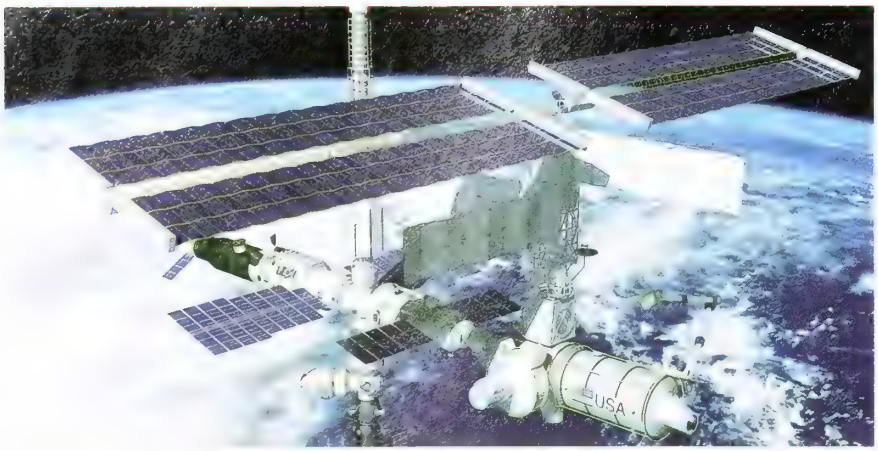
Bronfman and Meyer are working to fill other holes. Buying Interscope, which represents such artists as Dr. Dre and Tupac Shakur, will help revitalize a music unit that has broken few hot new acts recently. And expensive new rides based on the movies *Jurassic Park* and *Terminator 2* should juice up MCA's theme parks in Los Angeles and Orlando, where attendance is suffering.

But Meyer and Bronfman still must restock a studio that had grown overly reliant on Spielberg. Starting in 1997, the director will make films for the DreamWorks SKG studio he started with Geffen and Jeffrey Katzenberg; MCA will get just a small distribution fee. "Every time I see Edgar, he says, 'Produce more, produce more,'" jokes Howard's longtime producer-partner, Brian Glazer.

Bronfman may recruit still more pricey talent. Rumors persist that former Viacom Inc. CEO Frank J. Biondi Jr., who lunched recently in New York with Bronfman, will join MCA to fill the still-vacant chairmanship. With Biondi on the team, Bronfman may consider buying a broadcast network to expand Universal's distribution. That could help jazz up MCA's profits, which rose just 6% in the third quarter, to $221 million before taxes. "If we could do no more than bring MCA's profit performance up to industry norms, we could double the value of the company," Bronfman said at a recent industry conference. His checkbook is still open.

By Ronald Grover in Los Angeles

PHOTOGRAPH BY TIMOTHY WHITE/CPI



TAKING WING: *A computer simulation of the international space station*

TECHNOLOGY

LIAR'S POKER HIGH IN THE SKY

How the Russian Space Agency imperiled the space station

Back in 1994, Washington drew a line in the heavens. NASA had just completed yet another redesign of the troubled space station. Both Congress and NASA's tough-talking administrator, Daniel S. Goldin, vowed that either the new version would soar into orbit—or forever stay grounded. "We're done redesigning the space station," he declared. Change the $17 billion project again, "and we'll lose it."

That looked like a distinct possibility in November, when project partner Russia dropped a bombshell: It wanted a costly redesign. As Goldin and station supporters held their breath, Russian engineers suggested substituting their old Mir station for sexy new hardware. But as it turns out, the proposal was a cagey gambit to extract more funding for their own space efforts. The cosmic crisis wasn't finally resolved until Jan. 29, when Russian Prime Minister Viktor Chernomyrdin met with Vice-President Al Gore at the White House. The two agreed that the U.S. would help the Russians by adding three space shuttle flights to service Mir and launch key Russian space station hardware in return for Russia moving forward with the original design.

Here's the tale of how behind-the-scenes Russian maneuvering almost killed the massive project, 12 years in the works. Until the scare, the space station project seemed finally to be flying high. Joint missions between the U.S. space shuttle and Mir had been a success, paving the way for the larger international station. And in October, reluctant European nations agreed to commit to their share of the effort (table).

MIR VANITY. Then came Russia's stunner. At a November meeting in Moscow, Russian space chief Yuri N. Koptev told NASA space station chief Will Trafton his agency faced an intractable problem. Thanks in part to recent upgrades, he said, Mir is expected to last a decade longer than planned. For political reasons, the Russian Space Agency couldn't shut it down. But neither could the agency both operate Mir and pull its weight on the U.S.-led station, in part because it hadn't gotten its full $300 million budget from Moscow. In fact, a shortfall of tens of millions of dollars had caused space company Khrunichev to fall six months behind in building the service module, scheduled for launch in April, 1998. So, asked Koptev, why not scrap the new hardware and redesign the station around Mir?

That posed a threat to the station, especially given its already tight budget, ambitious schedule, and erratic political backing. Goldin was in a panic, says F. James Sensenbrenner Jr. (R-Wis.), chairman of the House space subcommittee: "I told him emphatically that the proposed redesign would cost at least six months and $1 billion to $2 billion—and that there would be no support in Congress for that." Goldin implored Sensenbrenner and NASA's appropriations committee chair, Representative Jerry Lewis (R-Calif.), to go to Moscow to plead the U.S. case.

Meanwhile, NASA engineers scrambled to find a solution. Their proposal: Stick to the original design but give the Russians more support. NASA could substitute shuttle missions for Soyuz flights, for example, to service Mir and the new station. While the Russians mulled this idea, Sensenbrenner and Lewis met with Deputy Prime Minister Oleg Soskovets on Jan. 9. Soskovets agreed to drop the Russian proposal in favor of NASA's approach. And he vowed to immediately send contractor Khrunichev the $10 million it needed to pay its subcontractors—and get the crucial service module back on track. "This was one of those congressional junkets that actually saved taxpayers money," says Sensenbrenner. Later in January, a team of Russian engineers flew to Johnson Space Center in Houston to hammer out the technical details in time for the Gore-Chernomyrdin summit.

Russian space officials now admit what many in the U.S. suspected: The Russians' main goal was never to radically alter the space station or wrest major concessions from the U.S. Instead, the Russian Space Agency proposed a dramatic redesign in part to use the weight of Congress and NASA to pressure Moscow into fully funding its own space effort. The ploy worked. But the space agency was playing Russian roulette with a major scientific venture.

By John Carey in Washington, with Geoff Winestock in Moscow

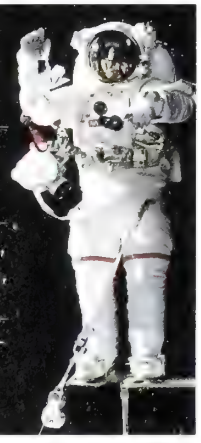
ZERO-GRAVITY COOPERATION

Which countries are doing what work on the space station

UNITED STATES is responsible for the crew quarters, a lab module, truss, and the solar array.

RUSSIA is building a service module, propulsion systems, docking modules, and the emergency return craft.

OTHER Japan and Europe are providing laboratory modules. Canada has charge of the robotic arm.



EDITED BY KEITH H. HAMMONDS

IT NOVELL, THE WORD IS BLUNDER

NOVELL FINALLY ABANDONED former chairman Raymond Noorda's worst mistake. The software maker, under Noorda's command, paid a whopping $855 million in 1994 for WordPerfect. It unloaded the unit, and its Quattro Pro spreadsheet, on Jan. 31 for just $186 million in stock and cash. The buyer: Corel, a $196 million Ottawa-based graphics software company in which Novell will take a 20% stake. It's a fire sale, all right—but analysts still question Corel's judgment. Corel hopes to tap into WordPerfect's 15 million customers and says the purchase broadens its software offerings. But analysts point out that the strength of Microsoft's rival Word program makes WordPerfect's future cloudy, at best.

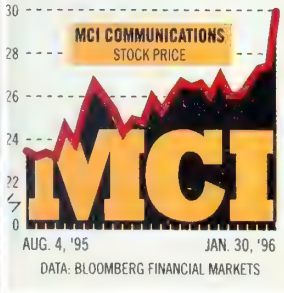
MURDOCH TAKES AIM AT 'LEFTISTS'

WHEN RUPERT MURDOCH doesn't like what he sees on TV, he doesn't just reach for the remote. He started Fox as an antidote to the Big Three networks. Now, he's launching a 24-hour cable news channel to counter what he sees as the leftist leanings of Cable News Network. On Jan. 30, he hired to head his new venture Roger Ailes, the former Reagan operative who departed CNBC, NBC's business news channel, earlier in the month. Murdoch says he plans to spend $80 million a year on news gathering and to have his channel up and operating by Election Day.

CLOSING BELL

MCI SAYS, 'WOW!'

How's this for a few days' toil? On Jan. 26, MCI Communications announced it had bought an orbital parking spot, paying $682 million with News Corp. for a license to offer satellite TV service across the U. S. Three days later, the long-distance company revealed a broad partnership with Microsoft. Then came the capper: strong fourth-quarter profits of $284 million, up 18% from last year. It was that, mainly, that sent long-sluggish MCI shares up 6.4% on Jan. 29, to a 52-week high of 29¼.



PAN AM IS BACK—SORT OF

IT ONCE WAS THE MOST glamorous name in the skies. Now, Pan American World Airways is going deep-discount. An investor group that paid $1.3 million for the liquidated carrier's logo announced plans on Jan. 30 to serve four cities this summer from New York. CEO Martin Shugrue, a former Pan Am executive, expects the new airline will keep operating costs one-third lower than Southwest Airlines and other discount rivals by outsourcing some functions, using efficient Airbus A300 planes, and sticking to long-haul routes.

WHY IBM PAID SO MUCH FOR TIVOLI

IBM MAY NOT WANT APPLE, but it's willing to pay top dollar for an obscure software developer. On Jan. 31, it agreed to buy Tivoli Systems, a $50 million provider of software to manage computer networks, for $743 million. That's $47.50 a share for a company that went public last March at $14. Why does IBM so urgently want Tivoli? Big Blue leads in managing mainframe computers but lags in administrating network applications. Consultant Judith Hurwitz estimates that building a product like Tivoli's could take IBM five years. "They need something right now," she says.

HEADLINER: G.I. JOE

MATTEL'S BOY-TOY PLAY

Figuring out girls has never been the problem for Mattel: Sales of Barbie, for one, have shot to $1.4 billion from $430 million in the past decade. But boys—the toy company just can't get them right. Its latest action figures have gone nowhere.

That's why Mattel so wants to merge with Hasbro, its arch-rival. Hasbro's G. I. Joe is the all-time boy-toy king, and the company has cleaned up with figures based on *Batman* and *Star Wars*. Such toys produce gross margins of about 60%. So do board games, which Hasbro dominates.

Mattel Chairman John Amerman is trying to push Hasbro into a $5.2 billion stock deal. But sources say Hasbro Chairman Alan Hassenfeld, hurt that Amerman won't anoint him successor in a combined company, has lobbied pals in Washington and Hollywood to protest the deal's antitrust implications. Amerman likely won't back off: He dearly wants Joe in his army.

By Eric Schine

LOEWEN NARROWLY MISSES A FUNERAL

LOEWEN GROUP ESCAPED THE Mississippi court system relatively unscathed. On Jan. 29, it agreed to pay $85 million, after taxes, to settle a suit brought by a local funeral parlor operator who had charged Loewen with breach of contract. True, British Columbia-based Loewen, North America's second-largest funeral home operator, did walk away from an agreement to buy two homes. But although the initial suit sought just $25 million in damages, a Mississippi jury last fall ordered Loewen to pay $500 million in damages. The state Supreme Court ruled the company would have to post a $625 million bond to proceed with an appeal. Faced with the prospect of Chapter 11 bankruptcy, Loewen settled. Relieved investors sent the stock up 42%, to $29.

ET CETERA . . .

- Digital Equipment, having failed to make a dent, will quit the home-PC business.
- Reader's Digest will cut 1,000 jobs and take a charge of up to $225 million.
- Sales of Prozac, Eli Lilly's antidepressant drug, jumped 24% in 1995, to top $2 billion.
- www.thinmint? Boston Girl Scouts now have their own cookie-order Web site.

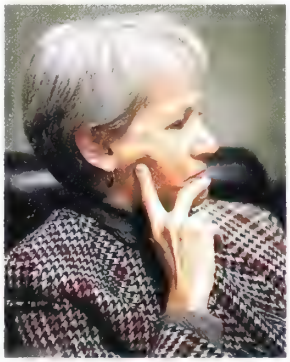
EDITED BY OWEN ULLMANN

HEALTH-CARE REFORM: THE PATIENT IS STILL BREATHING

Not long ago, it looked like health-care reform was terminal. After all, Republicans buried President Clinton's ambitious reforms in 1994. And Clinton returned the favor this winter by rebuffing the GOP's balanced-budget plan because of larger cuts in the projected growth of Medicare and Medicaid than the President would accept.

But hold on. With budget talks in limbo, some lawmakers fret they'll have to face voters in November with nothing to show for their efforts. So a bipartisan effort is under way in Congress to pass modest health reform this year. And this time, thanks to a push from Corporate America, the drive may succeed.

MANY CHEERS. The measure under discussion would protect the millions of Americans who fear losing health insurance by switching jobs. The bill would guarantee workers the right to obtain health insurance as they move from job to job, whatever the cause. It's a popular idea. Indeed, Clinton's Jan. 23 State of the Union message got loud applause from both sides of the aisle when he urged lawmakers to help people "buy health insurance policies that they do not lose when they change jobs or when someone in their family gets sick."



KASSEBAUM: *A legacy?*

In the Senate, a reform bill stalled since August may be breaking free. A band of conservative senators who had secretly blocked a vote appears to be relenting. Meanwhile, in the House, Representative William M. Thomas (R-Calif.), chairman of a Ways & Means health subcommittee, supports a similar measure. Both bills would limit insurers' ability to deny coverage because of pre-existing medical conditions. The Senate version also guarantees laid-off workers the right to buy individual coverage—though perhaps at higher rates—after their company benefits end.

The proposals have broad support because they don't cost the government any money. The Senate version, sponsored by Labor Committee Chair Nancy L. Kassebaum (R-Kan.) and ranking Democrat Edward M. Kennedy (D-Mass.), sailed through the committee unanimously. Business groups, including the National Association of Manufacturers and the U.S. Chamber of Commerce, endorsed the plan. "It will enhance our productivity by letting workers move around," says Julie Cantor-Weinberg, an NAM official. The National Federation of Independent Business, normally hostile to regulation, liked a provision that lets employers and workers form purchasing cooperatives to bargain for lower rates. But the bill stalled as Congress focused on passing a balanced-budget blueprint.

The failure to cut a budget deal has given health-care portability new momentum. And micro-reform seems to be faring better than Clinton's original grand scheme. Last year, Congress restored a tax deduction for self-employed persons who buy health insurance. If lawmakers approve the additional changes, Republicans "could go to the voters and honestly say they've done health reform as they once defined it," says Michael J. Langan of Towers Perrin, a New York management-consulting firm.

Insurers aside, the corporate community is cheered by the bill's prospects. Business groups say unwillingness to shift jobs for fear of losing health coverage reduces the hiring pool of top people. The General Accounting Office estimates that 25 million Americans are frozen into jobs because of pre-existing medical conditions or fear of losing benefits.

Still, the reforms could be scuttled by liberals who want costly changes—mandates that expand coverage for mental health, set minimum maternity hospital stays, and raise caps on lifetime payouts. And some conservatives oppose reforms. But Kassebaum, who is planning to retire this year, is pushing to make a modest health bill her parting legacy. If she and the Democrats can hold their left and right wings in check, reform could be a strong bet.

By Paul Magnusson

CAPITAL WRAPUP

THE IRS'S TAXING 800 NUMBER

▶ Looking for somebody at the Internal Revenue Service to help you with tax problems this year? Be prepared to wait . . . and wait . . . and wait. Budget cuts have savaged the IRS's telephone-assistance line. There are alternatives, such as a system of recorded phone advice and help via the IRS's new Internet home page. But to reach a live representative, "people are going to have a harder time getting through," concedes an agency spokesman. He got that right: BUSINESS WEEK called the IRS 800 number and spent 28 minutes on hold before giving up. And the filing season is just getting started.

QUAYLE'S QUALMS

▶ With GOP Presidential front-runner Bob Dole's polls ebbing, former Vice-President Dan Quayle has been telling friends he erred by forgoing the race. Had he stayed in, Quayle boasts, he'd be neck and neck with Dole. But confidants think the ex-Veep is deluding himself. Figures one: "He'd be lucky to get 4% of the vote."

TV THREAT: YOU'LL PAY FOR THIS!

▶ The nation's television broadcasters plan to use—what else?—commercials to fight Senate Majority Leader Bob Dole's proposal to make them pay up to $70 billion for new airwaves carrying digital signals. The National Association of Broadcasters' multimillion-dollar campaign is expected to hint that free TV may go down the tube if Congress charges billions for the new spectrum. Station owners also are lobbying members of Congress to oppose Dole's scheme.

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CHINA

ITCHING TO JAB BEIJING

With Congress spoiling for a showdown, trade may suffer

Representative Frank R. Wolf feels betrayed. Last year, the conservative Virginia Republican, a longtime critic of Beijing, swallowed hard to back continued U.S. trade ties with China. But the White House can count Wolf out this year. Outraged by China's bellicose behavior and President Clinton's vacillating response, he is whipping up support for linking Chinese trade privileges to Beijing's human-rights record. Vows Wolf: "We will make sure people have to confront issues such as China's persecution of Catholic priests and the starvation of children in China's orphanages."

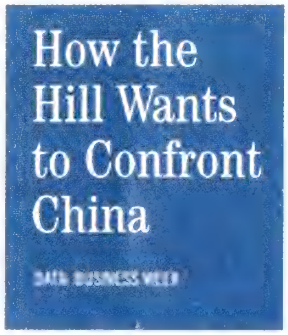
Wolf's statement is just one sign of Capitol Hill's hardening toward China. "We're bracing for a battle royal," says one Administration official with a sigh. After the 1989 Tiananmen Square massacre, Congress used the annual review of China's most-favored-nation (MFN) trade status to pressure Beijing to improve treatment of its citizens. In 1994, Clinton broke with congressional China critics and unhitched MFN from human rights. But election-year politics, Administration missteps, and provocative moves by China now virtually guarantee a showdown.

UNCHECKED PIRACY. U.S.-China relations, already strained, are ready to take more hits. Republicans and Democrats alike are urging the White House to punish Chinese transgressions on human rights, trade, and Taiwan (table). An early flash point will be the one-year anniversary in February of a U.S.-China accord to police intellectual piracy in the Middle Kingdom. Egged on by Congress, U.S. Trade Representative Mickey Kantor is threatening to slap more than $2 billion in sanctions on Chinese exports for Beijing's failure to halt copyright ripoffs. Says one senior Administration official: "If you aren't serious about enforcing basic trade agreements, [why] would China think you're serious about enforcing other commitments?"

China's threats to attack Taiwan are another hot issue. In late January, Chinese Premier Li Peng warned that Beijing will make reunification with Taiwan a top priority after China resumes control over Hong Kong next year and Macao in 1999. At the same time, the U.S. revealed that in December the aircraft carrier USS Nimitz sailed through the Taiwan Straits in a thinly veiled message to Beijing. Most worrying to many China-watchers is a possible invitation to Taiwanese President Lee Teng-hui to address Congress after his likely reelection on Mar. 23. Lee's visit to Cornell University last June shook U.S.-China relations for months.

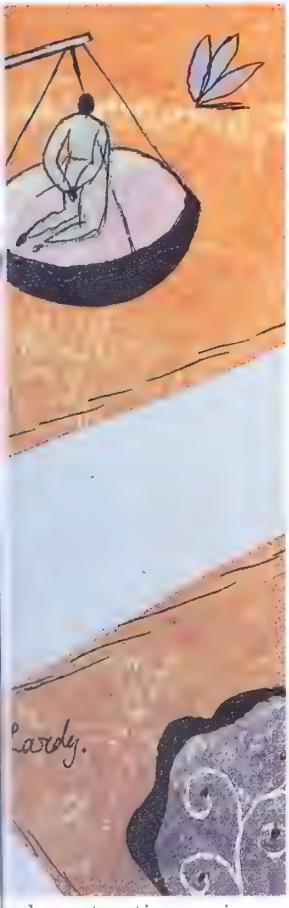
Congress' increasingly hostile stand on China contrasts sharply with the enthusiasm of Corporate America for the world's most populous country. More and more companies view China not just as a promising market but a critical one. Many multinationals that have been patiently building bases there are making money for the first time. Turbulence between Washington and Beijing could rock U.S. business plans. A major disruption in trade—or retaliation by Beijing in the form of shunned deals—would be devastating. "What we see is a colossal discordance between the rhythms of global business and American politics," says Robert A. Kapp, president of the U.S.-China Business Council.

Even so, many American executives shrug off the latest signs of tension. "There are plenty of bumps on the road, but the potential is so enormous that you can't ignore [China]," says Jean-Pierre Rosso, president of Case Corp., a Racine (Wis.) maker of farm



PIRACY

Will back imposi sanctions on Ch for failure to pro tect software, co pact disks, and other intellectua property



Clinton's carrot approach with Beijing hasn't worked well, and now it's payback time for the Republicans, who remember how he blasted Bush in 1992 for coddling dictators

ıd construction equipment. Case just osed on a $3 million joint venture in hina's southern Guangxi province to ıild backhoes and is racing to start roduction there. Case has plenty of ompany. U.S. direct investment in hina grew at a 16% clip in the first ne months of 1995, a slowdown from ıe fourfold jump of 1993 but still brisk.

ETO-PROOF? Corporate America's non-ıalance toward China tensions is un-erstandable: Business has weathered ırker periods in Sino-American rela-ons, such as the aftermath of the ananmen Square massacre. And until st year, the battles over MFN were an pected rite of spring in Washington.

Still, some China-watchers worry at executives are in a state of denial about the potential dangers lurking in Congress' increasingly harsh view of China. "If business goes to sleep on this issue, as they look set to do, the White House could be really exposed," warns a trade adviser to the Administration. The worst-case scenario: Congress votes to disapprove MFN for China, leaving the President with scant political cover for a veto.

Capitol Hill's latest bout of China fever has as much to do with politics as policy. Within the Republican Party, realpolitik free-traders are losing ground to moralistic economic nationalists. While many GOP freshmen have scant interest in foreign policy, recent reports detailing the pitiful plight of Chinese orphans are resonating with congressional newcomers on the Christian right.

Meanwhile, centrist Democrats who support free trade lost big in 1994, and more are dropping out of politics. That has tilted the Democratic caucus more toward liberal opponents of China's MFN status. "We used to have a reasonably good bipartisan approach" to China, says Representative Robert T. Matsui (D-Calif.) "On both sides, you're seeing a significant shift."

China policy is a can't-miss opportunity for Republicans to turn the tables on Clinton, who blasted George Bush in 1992 for coddling dictators. In 1994, Clinton reluctantly uncoupled MFN from human rights, promising to use other diplomatic tools to pressure China into treating its citizens better. That hasn't worked. Beijing's leaders have been cracking down ruthlessly on dissenters as they jockey to succeed the ailing Deng Xiaoping.

Frustrated, China's critics in the House are pressing the Administration to rally international support behind a vote to censure Beijing at a meeting of the U.N. Commission on Human Rights (UNCHR) in March. Clinton's foreign-policy team tried last year, but its robust lobbying effort—Vice-President Al Gore and National Security Adviser Anthony Lake worked the phones frantically—failed by one vote. Rights advocates worry that the White House may make only a pro forma effort this year. "I am afraid the Administration has written off some countries as being nonsupportive," says Representative Nancy Pelosi (D-Calif.), co-sponsor of a resolution urging the U.S. to take on China at the UNCHR meeting.

While Beijing could shrug off a bad report card from the U.N., it would be enraged by any move by Congress to shore up ties with Taiwan. Yet China's recent saber-rattling toward the island, which Beijing regards as a renegade province, is courting precisely the kind of congressional reaction the communist leaders fear. Senator Frank H. Murkowski (R-Alaska) and fellow GOP friends of Taiwan are considering steps to reaffirm and even strengthen U.S. support for the island democracy. "We are right to restate our commitment to provide arms for Taiwan's self-defense," Murkowski says.

POLICY VACUUM. The Administration bears some of the blame for congressional unruliness on China. The White House's failure to devise a coherent strategy for managing relations with Beijing created a policy vacuum that hard-liners in Congress have rushed to fill. For all the Administration's talk of its commitment to "constructive engagement" with China, Beijing hard-liners view U.S. policy as concerted containment.

That's not likely to change. As the '96 campaign heats up, Clinton will try to finesse charges that he's soft on China. That may not be easy. With the Middle Kingdom quickly supplanting the Evil Empire as Global Menace No. 1 in the minds of U.S. politicians, the President's rivals are sure to milk the issue for all it's worth.

By Amy Borrus, with Stan Crock, in Washington, Joyce Barnathan in Hong Kong, and Dexter Roberts in Beijing

AN RIGHTS	TRADE STATUS	ORPHANAGES	TAIWAN
essure the Administra- vigorously nembers of N. Commis- Human to censure next month	Will attempt to deny most-favored-nation privileges for China and restore the link between trade and human rights that Clinton ended in 1994	Will push for an international investigation of reports that orphans are systematically allowed to die	Will push for deeper support of democratic island, including possibly inviting President Lee Teng-hui to Washington

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BOOK FOR WHOEVER YOU HAPPEN TO BE.

You still have the invitation to your 7th birthday party. (And you know where it is.)

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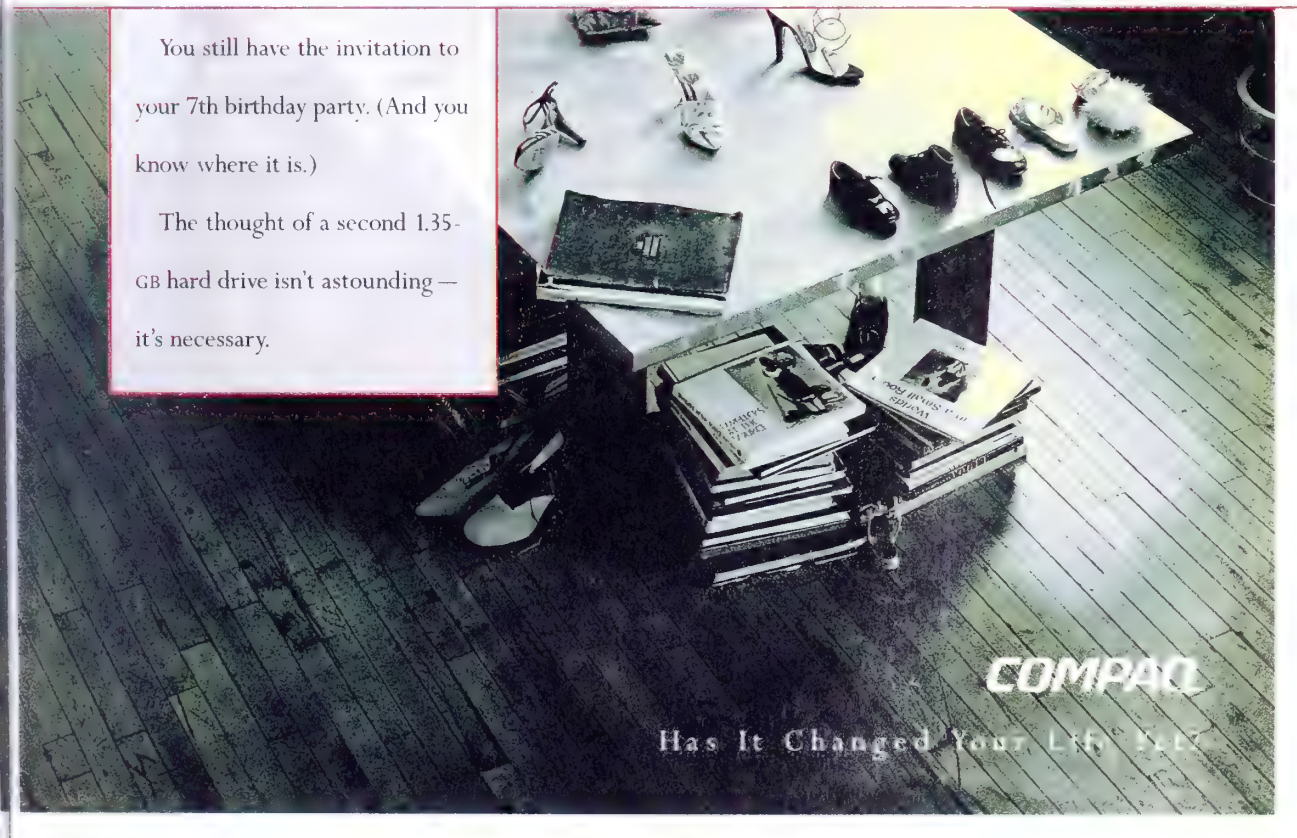

CASH-STRAPPED: *The company's losses for 1995 were nearly $1 billion*

ITALY

DE BENEDETTI AT THE BRINK

He promises he'll turn around Olivetti by yearend–or quit

Olivetti Chief Executive Carlo De Benedetti is working against time. Hailed as Europe's highest-flying technology entrepreneur in the 1980s, he is now struggling to save both his company and his job. With losses mounting for the fifth year at the $6 billion [illegible] group, De Benedetti has promised to turn its computer operations around by yearend or quit. "I am prepared to take the [illegible] willing to do," he told BUSINESS WEEK.

The situation is dire. Just two months after raising $1.4 billion in an international share offering, the company announced on Jan. 23 that 1995 losses would be larger than expected, close to $1 billion. Altogether, the company has lost $2.4 billion since 1990, largely because its computer business has not kept pace with technological changes. The stock price has been declining since early 1994 and plunged 15% in Milan, to a record low in late January (chart). In a make-or-break strategy, De Benedetti hopes to stanch the red ink while building Olivetti's new and potentially profitable telecommunications ventures.

With only 15% of the stock in his own hands, De Benedetti does not own enough of the company to prevent his ouster if shareholders demand it. New institutional investors such as Deutsche Bank and Baring Asset Management will wield unprecedented clout, especially after the dissolution in late January of a longstanding pact that allowed De Benedetti to tightly control the company. "This time, no results and he's out," says one British fund manager.

De Benedetti is making some progress. In computers, he has pushed the breakeven point down to 900,000 units, compared with 1 million a year ago. That's largely because he cut the workforce from 4,000 last June to less than 2,000 today. Still, margins are under pressure as more nimble players such as Compaq Computer Corp. grab market share.

To build a cash cushion, De Benedetti is seeking a partner for Olivetti's profitable computer systems and services business in Europe. He is also readying a sell-off of shares in Olivetti's $2 billion-a-year office-products unit, Lexikon, by the end of the year.

The extra cash will come in handy because profits from the company's new telecom ventures won't start rolling in for a couple of years. Olivetti is betting big on Omnitel Pronto Italia, Italy's No. 2 mobile-telephone operator, in which it owns a 59% stake with other investors. Omnitel is unlikely to make a profit before 1998, says its managing director, Francesco Caio. The good news is that Olivetti's stake in Omnitel is already worth around $2 billion. That's just about equal to Olivetti's entire market capitalization.

"STRANGE ELEMENT." Meanwhile, Olivetti has teamed up with Bell Atlantic Corp. and France Télécom in the hopes of cashing in on the liberalization of data transmission and long-distance services in Italy and throughout Europe. With the state-controlled Telecom Italia still providing shoddy service at high cost, Olivetti should do well, says Vito Morawetz, an associate at London's Cambridge Strategic Management Group. After deregulation, "it's hard to imagine someone not making money in this market," he notes.

That, of course, is what De Benedetti is hoping. But if Olivetti can't show a profit this year, he probably won't be around to claim the credit. In the nearly 20 years since he took over the struggling Olivetti typewriter firm in 1978, De Benedetti's career has been a roller-coaster. In the '80s, he made headlines for his attempted takeover of Belgium's largest conglomerate, Société Générale de Belgique. In the '90s, he faced corruption charges and fines for his alleged role in the 1983 fall of Banco Ambrosiano.

The way De Benedetti tells it, he gets no respect in Italy anymore. "I guess I'm probably a strange element in this country," he admits. It may be that De Benedetti's fellow Italians no longer accord him the accolades they once did. The only way he can change that is to get the black ink flowing again at Olivetti. It may be mission impossible.

By John Rossant in Rome, with Gail Edmondson in Paris

COMMENTARY

By Geri Smith

ZEDILLO HAD BETTER CLEAN UP THE CESSPOOL

Things in Mexico keep getting curiouser and curiouser. This time, a close associate of Raúl Salinas, brother of former President Carlos Salinas de Gortari, is saying that the $84 million discovered in Raúl's secret Swiss bank accounts is really a venture-capital fund. Carlos Peralta, a prominent Mexican businessman, says he gave Raúl $50 million to invest in tourism projects that never happened. Peralta never asked for a receipt and can't remember what bank he put the money in. Peralta denies any link between the $50 million and blessings such as a valuable cellular phone concession that were bestowed on him by the Salinas administration.

Peralta is a long-time friend of the Salinas family and controls Mexico's second-largest telecom company, Grupo Iusacell. Until now, he has shown excellent business sense. But he was apparently willing to look naive, perhaps to save his buddy Raúl's skin and win back the millions the Swiss seized as suspected money-laundering proceeds. Raúl has been jailed since March, 1995, on charges of masterminding a political killing 1½ years ago.

BIG DEAL. The Mexican public, of course, believes that Raúl Salinas' money came from business executives buying favors from his brother. If Raúl squirreled away that much, people figure, how much did other members of the Salinas team pocket? Both Salinas brothers deny any improprieties.

President Ernesto Zedillo Ponce de León has made a big deal about bringing the rule of law to Mexico. Now, he has to go beyond high-profile jailings and get to the bottom of the corruption quagmire, even if he must shake the political and business Establishment to the core.

The Mexican public wants a much fuller accounting. Foreign investors, whose resources Mexico desperately needs, want a more transparent business environment. Some of those who invested following the principle that the foreign partner provides the knowhow and the Mexican partner supplies the know-who could be in for sobering experiences. Bell Atlantic Corp., for example, has paid nearly $1 billion for 42% of Peralta's Grupo Iusacell since 1993 and has been stunned by Peralta's revelations. Bell Atlantic CEO Raymond W. Smith says his company has been over Iusacell's books with "a fine-tooth comb" and is confident the $50 million did not come from Iusacell since Bell Atlantic's involvement.

"WANTED": *A piñata of ex-President Salinas*

The big question is how far Zedillo is willing to push the investigation. The attorney general's office is investigating Raúl on charges of illicit enrichment, which could cover bribe-taking. But it's not clear whether the tax authorities intend to pore over Peralta's tax returns to see if he—or his company—reported the $50 million "investment."

The newly aggressive press and opposition members of Congress appear unwilling to let the scandal be swept under a rug. The excesses of the Salinas era have become a bitter national joke. Vendors in Mexico City hawk *piñatas* showing Carlos Salinas in a tuxedo brandishing fistfuls of pesos and dollar bills. Others sell dolls showing the former President dressed in prison garb and holding a sack of loot.

Sources confirm that Salinas is living in Cuba, shielded from prying eyes and investigators. Family members regularly trek to Havana to visit him—and the new baby just born to his mistress. But back in Mexico, many of the people that he and his brother Raúl dealt with while in power—businesspeople, politicians, and friends—are running for cover.

HONEST MAN. Peralta's disclosures sent real shock waves through several corporate boardrooms. He named other businessmen who he said may have contributed money to Raúl's mysterious fund: Adrián Sada of glassmaker Vitro and Banca Serfín and Roberto González of tortilla maker Maseca, who is Carlos Salinas' godfather. Both men immediately denied any connection with Raúl's millions.

There are several things Zedillo could do to help restore confidence. First, conduct a serious investigation into the origin of Raúl's accounts. If they are illicit proceeds from bribes for government favors, or payoffs from privatizations, such deeds should be punished. If South Korea is capable of going after top former officials and leading executives accused of bribery, surely Mexico can, too.

Second, Zedillo should set an example: He is widely believed to be an honest man who has not benefited illicitly from his government posts. Although he is not required by law to make public an annual statement of personal wealth, he could score big points by doing so.

Mexico's biggest problem right now is that its people do not trust their leaders. Most Mexicans assume that Zedillo will never get to the bottom of this scandal. If he is to win their trust, he will have to prove them wrong.

Smith heads the Mexico City bureau.

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YELTSIN TO VOTERS: REFORM? NEVER HEARD OF IT

To get an idea how Vladimir Kadannikov might handle himself as Russia's new First Deputy Premier for the economy, take a look at what he did in 1994. Flush with dollars, newly rich Russian capitalists were snapping up BMWs, Mercedes, and Volvos. They were sneering at the clunkers churned out by Avtovaz, the huge Russian carmaker where Kadannikov was chief executive. Instead of trying to spiff up his Lada models that look like 1972 Fiats, the car boss used his clout with Russian President Boris Yeltsin to slap a highly protectionist, 100% tariff on imported cars.

Kadannikov, whose rise accompanies Yeltsin's sacking of privatization chief Anatoli Chubais, isn't a total disaster. He has had substantial exposure to Western business practices and has a much more sophisticated outlook than some former Communist managers who have spent their careers in isolated arms plants. He has fans in the reform camp, including former economic honcho Yegor T. Gaidar. But this appointment is still a signal that Yeltsin was badly stung by the strong Communist showing in December's Duma vote. The President is focusing on the June presidential campaign, and he is going to try to distance himself from the pain of economic reform until that vote is over.

LADA LINE: *Tariffs shield the clunkers*

MISSING PAYCHECKS. Bringing in a Soviet-style factory director is intended to placate Russian workers and industrialists, who feel they have been shafted by reforms. Kadannikov can be expected to push for high tariffs and limits on privatization. Most worrisome, Kadannikov is also likely to throw big money at such political problems as failing industries and workers who aren't getting paid—a course that could reignite inflation.

Yeltsin's single biggest political problem is that millions of workers haven't seen a paycheck for months. Already, coal miners, schoolteachers, and metal workers are threatening to strike. Knowing that labor unrest could make a mess of his campaign, Yeltsin is setting up funds that would pay all workers one month's salary. He has also promised almost $7 billion for struggling industries. "Yeltsin is trying to distance himself from the pain that many Russians have felt during economic liberalization," says Liam Halligan, an economist at Moscow's Center for Economic Performance.

Such spending will be inflationary and won't address the real reasons why workers aren't being paid. One of these is the unchecked greed of enterprise managers who delay paying wages for three-month intervals. They then put the money in high-yield treasury bills and pocket the interest.

The primary difficulty is that many Russian enterprises have not been restructured and don't make enough to cover salaries. But Kadannikov will probably just prop them up rather than slim them down. Look at his own Avtovaz. Despite the high tariffs on imports, it still owes the government and creditors $1.2 billion and can't make payroll.

The prospect of blowing out the budget is already alarming Russia's international creditors. For instance, the International Monetary Fund, which had been preparing a $9 billion loan, is getting nervous. Sources say Prime Minister Viktor S. Chernomyrdin and Yeltsin are asking Western creditors to put up with a little backsliding that can be made up after the election. What the IMF may do is give Russia a more restrictive one-year facility instead of the planned three-year package.

The West is hoping that the Kadannikov era will be brief. He is there to help get Yeltsin reelected. If that goal is attained, Yeltsin will have much greater latitude to do as he pleases—the thinking goes. But it is becoming very difficult to determine what policies Yeltsin really favors.

By Patricia Kranz, with Peter Galuszka, in Moscow

GLOBAL WRAPUP

NEW MIDDLE EAST AIR WAR

▶ Jordan and Israel have made peace, but their national airlines are butting heads. Royal Jordanian is already offering Israeli customers cheap flights to the Far East from Amman. It has a competitive advantage over El Al Israel Airlines Ltd., because it can fly directly over Saudi Arabia. That slices about three hours off of flight time and several hundred dollars off the price of a ticket.

Royal Jordanian is expected to begin flying from Tel Aviv in a few weeks. Until then, local travel agents are offering Israelis deals involving bus trips across Jordan bridges and a one-day tour in Amman, combined with a flight to Bangkok and other Far Eastern destinations. El Al plans to fight back by offering travelers low-cost fares to Amman from North America via Tel Aviv.

BOSNIA'S BANKS CASH IN

▶ While European and American companies jockey for the business of helping rebuild war-torn Bosnia, one set of winners is already clear: local entrepreneurs who started private banks during the height of hostilities. The Clinton Administration and the World Bank want these lenders to handle the bulk of the anticipated hundreds of millions of dollars in loans to the private sector, which could start flowing as early as March. The private banks will get a boost from a financial system overhaul—aided by the U. S. Federal Deposit Insurance Corp.—whose aim is to close or sell off insolvent state-owned banks.

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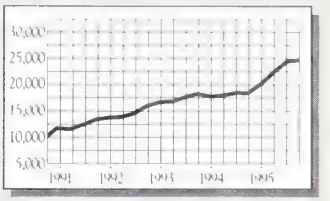

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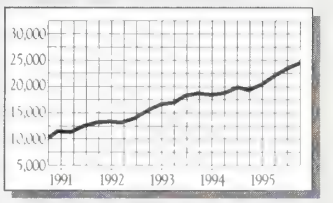

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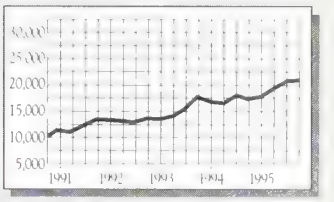

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STINGING SMALL BUSINESS

There's a new breed of swindler out there–and entrepreneurs are the prey

Back in 1993, Kreso Bezmalinovic was the proud owner of a thriving small business. The 46-year-old Croatian immigrant had carved out his own piece of the American Dream: In three years, he had built American Shipyard Corp. in Newport, R.I., into a $12 million company that repairs ships for the U.S. Navy and U.S. Coast Guard. But Bezmalinovic was soon to find just how precarious his hold on the entrepreneurial ladder really was. It was a lesson that would nearly put him out of business.

Scrambling to line up some much-needed capital, Bezmalinovic approached Onyx Financial Corp., a Miami-based firm that purportedly arranged financing. Assured that Onyx could raise $4 million, Bezmalinovic paid Onyx $50,000 in fees. But American Shipyard never received a dime. In August, 1995, Bezmalinovic may have found out why: Florida prosecutors arrested Onyx' principals on criminal charges of operating a fraudulent "advance fee" scheme to bilk three companies, including American Shipyard, out of $163,000. Meanwhile, the company struggled. The financial problems kept it from winning many new contracts, and sales slid 50%. "We got taken to the cleaners," says Bezmalinovic. "Thank God we survived."

For small businesses, Bezmalinovic's sad story, and variations on it, are becoming increasingly common. Small-business formation is booming, propelled by a generation of entrepreneurial innovators and the huge layoffs in Corporate America. But this eager class of risk-takers is discovering that the risks can be greater than they ever imagined. To all the normal bedevilments of small business—tight financing, unsure markets, strong rivals—add another: a new breed of unscrupulous moneymen who prey on entrepreneurs.

Special Report

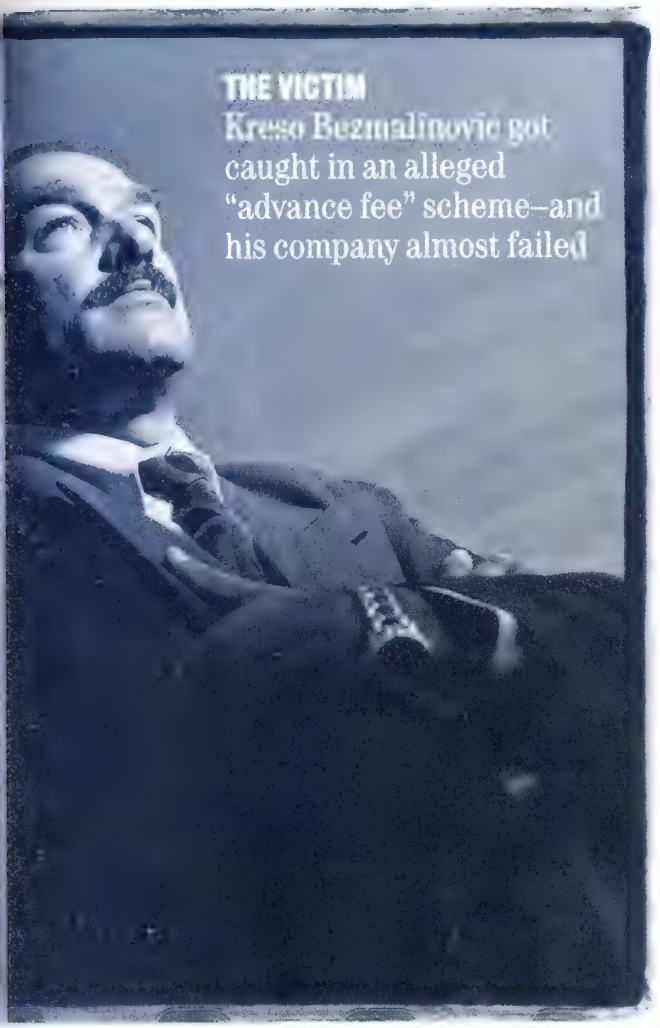
Con artists have been around for ages, of course. But the fatal combination of entrepreneurial fervor, need, and financial naivete makes small-business owners such as Bezmalinovic easy marks for a new variety of scamsters. Filled with enthusiasm for their own ideas, they can be startlingly inexperienced in finance. "Technical entrepreneurs, especially, think what they do is important, but that the business side is trivial," says Brad Bertash, director of the Wing-Brown Institute, a Salt Lake City nonprofit venture-capital consulting firm.

Above all, what makes emerging companies easy marks is their often desperate thirst for capital. Although Small Business Administration-guaranteed loans have expanded dramatically, companies that are further along in their development often fall through the cracks. Those needing $1 million to $10 million are too risky for traditional bank financing, while nonbank lenders can demand exorbitant interest rates. And most startups are not fast-growing enough for venture capital.

THE CON ARTISTS' TRICKS

	ADVANCE FEE SCHEMES	SHELL MERGERS
THE PITCH	An offer to help locate financing, such as letters of credit or capital from wealthy private investors.	A fast, cheap way to go p by merging with a nonope shell company that alrea shares trading.
THE CATCH	An up-front payment, usually $2,500 to $30,000. When the cash never materializes, promoters often blame the company's poor finances. In truth, the investors never existed.	The new company's stock languishes because inve are leery of tiny, unknown Shares are also ripe for m lation by brokers and exis stockholders.

HOTBEDS OF ABUSE. So entrepreneurs are left to swim in shark-infested waters: the world of stock promoters and brokerage firms that specialize in small-cap companies. Worse yet, well-intentioned efforts by the government to make it easier for small businesses to raise capital have paradoxically created hotbeds of abuse. Indeed, many of the schemes used to squeeze money from unsuspecting entrepreneurs are technically



THE VICTIM
Kresso Bezmalinovic got caught in an alleged "advance fee" scheme–and his company almost failed

cial predators are targeting capital-starved small companies host of sophisticated scams. A few of the more common ones:

IRM REGISTRATION

an SEC-sanctioned SCOR orm registration, companies ll shares faster and at less an a full IPO.

ers often charge huge fees to e SCORS, but results are often hey may oversell their services tential. Only 25% raise the ed sum.

GOING PUBLIC

Doing an IPO gives a small firm access to investors as well as the ability to finance acquisitions with stock.

Specialized small-cap broker-dealers often demand exorbitant fees And some unscrupulous broker-dealers then artificially inflate the stock; after they unload their own shares, the stock collapses.

DATA: BUSINESS WEEK

legal. Operating just this side of the law, many sophisticated promoters take advantage of loose regulation. "These guys are like tax attorneys, always looking out for new loopholes," says Howard Sirota, a former National Association of Securities Dealers investigator who now practices securities law. "They know exactly how far they can go to avoid trouble."

For Bezmalinovic, the problems began when the bank that held the mortgage on the waterfront site leased by American Shipyards got into financial difficulties and called the loan. Although he quickly lined up a replacement loan for $3.1 million, interest was a lofty 15½%. With the $39,000 monthly payments sapping cash, Bezmalinovic sought refinancing. He soon fell prey to one of the most common abuses small businesses now face: investment-consulting firms that demand fat up-

THE ACCUSED
Florida prosecutors say Onyx Financial's Walter Kolker (left) and Ronald Williams bilked Bezmalinovic and hundreds of others. Kolker and Williams have pled not guilty to charges.

front fees to look for funds. Such schemes typically target entrepreneurs who have exhausted personal resources.

A business acquaintance referred Bezmalinovic to Onyx, and he and his accountant flew down to meet Onyx principals Walter S. Kolker and Ronald G. Williams. In Onyx' lavish offices on prestigious Brickell Avenue in Miami's financial district, Bezmalinovic says, the pair assured him that they had many private investors on tap and financing would take just weeks. After calling a half-dozen references who sang Onyx' praises, Bezmalinovic paid Onyx $50,000.

He wasn't the only one apparently taken in: In November, 1993, Kolker and Williams were arrested and charged with taking fraudulent advance fees. Separate criminal charges of stock manipulation were filed in April, 1995. Beth Blechman, Assistant Statewide Prosecutor for Florida, says the evidence indicates that the pair has bilked some 250 client companies out of millions of dollars in a variety of scams. She expects further SEC civil charges to be filed soon. Moreover, Williams is a disbarred attorney who pled guilty to charges stemming from a fraudulent oil and gas tax shelter scheme in 1989.

Kolker and Williams have pled not guilty to the Florida charges. Kolker declined to comment. Williams, through his attorney, blames the risks of small business for financing problems. Meanwhile, with their trial delayed by procedural issues, they are still in business: They moved to new offices in the same building and reopened as Select Capital Advisors Inc.

FAMILIAR FACES. Sticking to the higher-profile, regulated world of IPOs may be no less risky. In recent years, a booming subculture has sprung up consisting of unscrupulous brokers eager to ensnare small companies in webs of linked transactions.

Ironically, they've emerged in part because the Securities & Exchange Commission did its job. The well-intentioned penny-stock regulations of the early 1990s now protect investors from the worst abuses of the bucket-shop scams of the '80s. But the con artists remain. Although such notorious firms as Blinder Robinson and First Jersey Securities have been shuttered, many penny-stock dealmakers and brokers are now working with small caps. "No question, many of the old penny-stock players have migrated," says Neal Sullivan, executive director of the North American Securities Administrators Assn.

One Houston firm is still reeling from such a scheme. Start-

IPO ORDEAL

Lisa and Joseph Turano fell victim to a stock-manipulation scheme that has left their legal-services firm unable to raise new capital

ing in the late 1980s, Lisa Moore Turano worked hard to build Co-Counsel Enterprises Inc., a provider of temporary attorneys and paralegals. The 41-year-old Turano, a Houston attorney, and her husband, Joseph Turano, 44, had offices in three cities by May, 1993, and wanted to expand. They met Joseph Pagano, a venture capitalist from Aspen, Colo.

According to the Turanos, Pagano offered to provide management and financing advice, as well as locate an underwriter, in exchange for a stake in Co-Counsel. They sold 25%—at a price of 48¢ per share—to a group headed by Pagano in July. Within months, the Turanos claim, Pagano helped arrange a $4 million public offering to be underwritten by J. W. Charles Securities Inc. in Boca Raton, Fla. On Nov. 22, 1993, Charles led the sale of roughly 1.6 million units—of one share and one warrant each—for $3.25. Within two weeks, the value of the units inexplicably shot up 150%, to $8. Then just as suddenly, the value dropped 60%, to $3 by yearend.

The price gyration caught the attention of the SEC. In October, 1994, it filed a civil complaint alleging stock manipulation against three brokers: F. N. Wolf, Hibbard Brown, and L. C. Wegard. All trace their lineage to First Jersey.

In its October complaint, the SEC alleged that within two weeks of Co-Counsel's IPO, the three acquired 95.7% of the shares. By trading among themselves, the SEC alleged, Wolf, Hibbard Brown, and Wegard pushed the shares to $8 before unloading them on retail clients. The shares have now fallen below $1. All told, the SEC alleged that the firms earned $5.5 million manipulating Co-Counsel's shares. Neither Pagano nor J. W. Charles were named by the SEC.

"DISTRACTION." How did virtually the entire stock offering get from J. W. Charles to the other brokers in two weeks? According to SEC officials, F. N. Wolf & Co. President Franklin N. Wolf arranged for a number of large investors to buy large blocks of the IPO directly from Charles and other brokers. Those investors then quickly sold the shares back to Wolf's firm for a small profit. Joel Marks, head of Charles's corporate-finance unit, denies any role in the manipulation. "We did nothing improper," he says.

Hibbard Brown & Co. settled the charges without admitting guilt, as did Frank Wolf personally. He was banned from the securities business for life. In January, an administrative judge upheld the SEC charges against L. C. Wegard & Co. and F. N. Wolf, the firm. The SEC has revoked the registration of all three firms. Wolf did not return repeated calls, nor did the attorney for Hibbard Brown. Jerry Selvers, an attorney for Wegard, denies any wrongdoing and says Wegard is still operating while it appeals.

Pagano vehemently denies any role in arranging Co-Counsel's IPO or in the stock manipulation. He says he was simply a venture-capital investor and provided no financing advice. Although Pagano admits he introduced the company to his longtime associate Wolf—whose wife participated in Pagano's pre-IPO investor group—he says he was unaware that Wolf's firm had been repeatedly cited for violations by the SEC or had links to First Jersey.

Although an innocent victim of the manipulation, Co-Counsel has been tainted. With its stock now trading below the exercise price for the IPO warrants, it has been unable to raise capital to complete its expansion. "It's caused distraction and damage," says Turano.

The scheme that hit Co-Counsel clearly violated securities regulations. However, one of the most common abuses small companies face appears perfectly legal. For many, the quickest route to financing can be the Small Corporate Offering Registration (SCOR). Designed by the SEC to make going public easier and cheaper, a SCOR is a shortened prospectus for registering stock offerings up to $1 million. So far, success has been mixed. Since 1992, the Dallas-based newsletter *SCOR Report* has recorded 547 offerings. But only about 25% have raised the planned funds.

The reason is that many such companies shouldn't be going public in the first place. Few serious investors would put money into unproven companies about which they've received only limited financial information. But financially naive entrepreneurs often don't realize that. Instead, they listen to a host of questionable advisers who charge huge fees to help firms file a SCOR—while vastly overselling the chances of success.

That was the experience of Kathy Kidder Jones, founder of Urinette Inc. in Pensacola, Fla. A former saleswoman for American Hospital Co., Jones, 47, designed a female urinal for use in public restrooms. By 1993, Jones's patented invention was a hit in test marketing. She outfitted a plant with $400,000 from friends and family but needed $700,000 for marketing.

A local stockbroker recommended that Jones talk with DMV Inc., a three-person consulting firm in Clearwater, Fla. Jones says that DMV CEO Leonard Toups persuaded her to do a short-form placement to raise the $700,000. His selling point, according to Jones: Toups promised to provide investors. "We decided to work with them because they said they had investors they'd bring to the table," says Jones.

That turned out to be only one of DMV's many misrepre

sentations, Jones claims. Since SCOR placements require firms to find investors themselves to buy their shares, DMV's services included advice on how to run a successful direct-marketing campaign to sell stock. Jones says Mark C. Clancy, DMV's compliance officer, advised her the process would take about four months and involve upfront costs of around $17,000, with an additional $40,000 in fees and expenses later. Clancy even gave Jones a copy of his book, *The Art and Science of Raising a Million in 120 Days.*

Jones didn't get anywhere near that much—and it took a lot longer than 120 days. The process consumed nearly a year and cost Jones $74,000. The offering raised only $360,000, virtually none of which came from DMV's purported investors or the direct-marketing campaign. "They completely oversold their capabilities," complains Jones.

Toups did not respond to requests for comment. Speaking for the company and himself, Clancy denies Jones's contention, saying she "is under miscommunication." He says that DMV's estimates for time and expenses were simply "best case." And he says DMV never promises to line up investors. But three other DMV clients contacted by BUSINESS WEEK say Toups made exactly the same promise to them. "They definitely told us they would bring investors to the table," says Robert M. Hickey, a principal of Joffrey's Coffee & Tea Co. in Tampa. But when DMV failed to produce any investors for Joffrey's $1 million offering, the company reaped just $150,000 from other sources.

SHELL GAME. Other seemingly legal money-raising schemes can have even more devastating results. One favorite of unscrupulous stock promoters: They resurrect inactive shell companies that already trade on NASDAQ and do "reverse mergers" by acquiring legitimate startups desperate for funds. Utah securities director Mark J. Griffin says he has seen a disturbing upsurge of such "zombie" shells. "They are usually the kiss of death," Griffin warns.

The reason: The promoters convince companies that after going public through a shell, they can easily raise cash by issuing more stock. They point out that shell mergers can be done for about $50,000 in a month, while SEC-registered IPOs cost $200,000 and take up to a year.

What the promoters don't bother mentioning is that such shells are also ripe for rip-off. Since they're typically small enough to escape the SEC's reporting requirements, such companies often don't report financial information, leaving them wide open to manipulation.

That was the situation Chuck Faylor found himself in 18 months ago. The aspiring cartoonist had chucked a 17-year career as a Sears, Roebuck & Co. salesman in Boise, Idaho, to launch Noah's Art, a line of humorous animal greeting cards. Using money from his nest egg, Faylor's four-man sales staff quickly placed the cards in 800 shops. But to expand, Faylor needed a larger sales force.

So Faylor was pleasantly surprised when Irving R. Rill, a congenial 73-year-old representing a Coral Gables (Fla.) company called BestSellers Group Inc., approached him at a stationers' convention in May, 1994. Rill wanted to buy Noah's Art. Faylor would stay on to run the card business, while BestSellers, which marketed books to gift shops through a sales force of 70, would handle marketing and finance. Faylor thought it a perfect fit. He sold Noah's Art to Rill on Dec. 30 for $38,000 and 100,000 shares of BestSellers, which he says Rill told him was set to go public in early January.

"I WAS NAIVE." But the 39-year-old artist appears to have ended up on the wrong side of a shell deal. In reality, Rill had acquired control of BestSellers on June 30, 1994, when he arranged for it to go public through a merger with a nonoperating NASDAQ-traded shell company, NACC Acquisition Corp. In compensation, BestSellers issued 6.4 million shares to Amerril Corp., a private company controlled by Rill.

BestSellers shares didn't begin trading until Jan. 13, 1995, when they showed up on NASDAQ's Bulletin Board, a market for small, thinly traded stocks. But Faylor says he never got the shares or cash he was owed. By late January, he says, he discovered the buyout was a sham.

Rill appears to have bought Noah's Art primarily to make BestSellers' stock look more attractive to investors. Faylor says he discovered in February that BestSellers could barely pay its own bills. And according to Faylor and two well-placed former BestSellers employees, Rill immediately cashed Noah's receivables and stopped paying its bills. Yet in financials Rill presented to brokers as he promoted the stock just before it appeared on NASDAQ's Bulletin Board, the company's value appears highly inflated. BestSellers forecast $1 million in revenues for Noah's Art for 1995—yet sales were just $80,000 in 1994. Rill also told brokers total 1995 revenues for BestSellers Group would be $16.7 million, including $9 million in sales from two other mergers that never took place. The share price hit $3.50 in late January but has since fallen to 20¢.

Rill did not return repeated phone calls. Speaking for the company and for Rill, BestSellers President Douglas G. Morgan denies any financial improprieties. He claims that the three ac-

BILL OF GOODS? Kathy Jones says consultants claimed they'd help her raise cash to market "urinettes," but their promises didn't pan out

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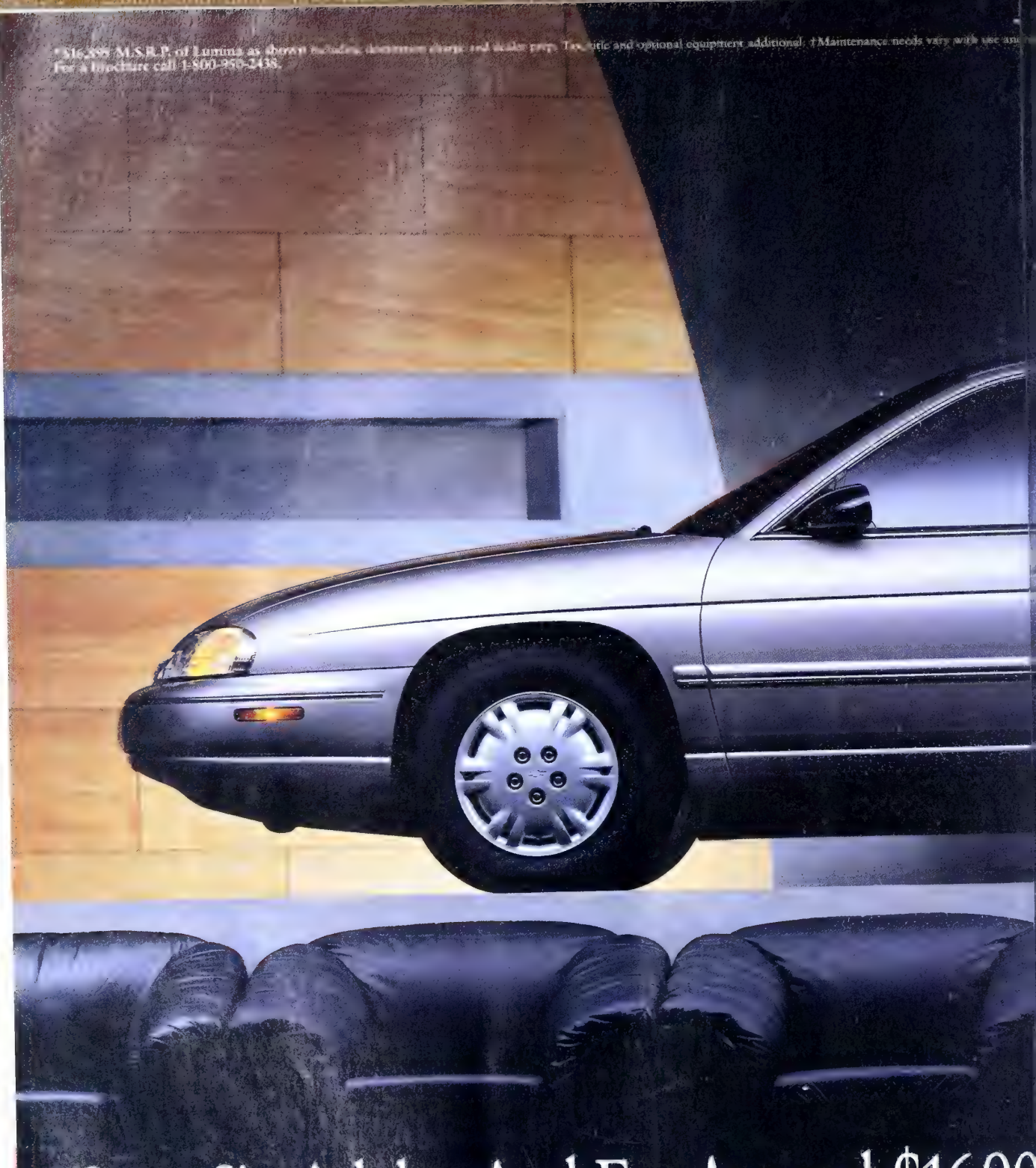

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quisitions simply didn't work out. According to financials supplied by BestSellers, the company reported no sales for the fiscal year ended June 30, 1995, and a net loss of $289,429.

BUSINESS WEEK has learned that there is more to Rill. According to the Drug Enforcement Administration, Rill was convicted in Queens (N.Y.) federal court in 1981 of conspiring to manufacture methaqualone, a depressant known as Quaalude. He was sentenced to probation and fined $15,000. And William R. Bohar, an investigator with the Florida Controller's Office, says that Rill shared offices with the principals of the former Onyx—the firm that allegedly defrauded American Shipyard—several years ago. Investigators believe they were business associates. Rill, through his lawyer, denies that, saying only that his late wife once shared offices with the Onyx principals.

Special Report

Morgan says Rill has now left BestSellers' board and is no longer involved with management. However, D. David Cohen, Rill's attorney, acknowledges that Rill's Ameril Corp. remains a major shareholder and "he continues to seek financing and other transactions for BestSellers."

The upshot for Faylor: With no income, he had to lay off his workers and shut Noah's Art. Creditors still hound him for bills that he says BestSellers never paid. He's now looking for a job. "BestSellers took our company and sucked the life out of it," he says. Idaho is investigating for possible securities violations. "I was naive," Faylor admits. "I don't think I can trust anyone again."

HIGH AND DRY
Chuck Faylor sold his startup, Noah's Art–only to discover that the deal may have been part of a complex stock scam

Another effort to simplify capital-raising that has often gone awry: Regulation S shares, named for an SEC regulation intended to make it easier for large companies to sell stock abroad. But in recent years, scamsters have used Reg S to lure small companies. "It's clear to everyone in the trenches that Reg S has become the domain of questionable investors and brokers," says Jesse M. Brill, corporate counsel to Dean Witter Reynolds Inc.

PHONY CHECK. Cash-starved Evans Environmental Corp. found out the hard way. Charles C. Evans, 39, had run a successful environmental consulting firm since the mid-1980s. But a poor acquisition in 1993 left it struggling. Early in 1994, however, Evans' troubles seemed to be solved when Harry DiFrancesco, president of National Equities Corp. in Fort Lauderdale, offered to arrange a Reg S deal: Evans says DiFrancesco promised to sell a big chunk of preferred stock to a Peruvian investor. Evans received a Bank of America cashier's check from Rosauro Santiago for $1,294,385 in exchange for 425,000 shares. For DiFrancesco's role, Evans paid a fee of $151,000. There was only one problem: The BofA check was phony. Although Evans eventually got the shares back, DiFrancesco kept his fee. The FBI and Miami police are investigating. Through his attorney, DiFrancesco declined to comment. Santiago could not be found.

That's just one type of Reg S problem. Others arise because foreign investors have to hold their shares for only 40 days. But since the shares are usually sold at discounts of up to 40% from their U.S. value, they're often dumped back in the U.S. for a quick profit. Brokers and short-sellers often make matters worse by selling the shares short in anticipation of the fall. Though legal, the ensuing share-price drop hammers existing investors.

Zycad Corp. in Fremont, Calif., saw the downside firsthand. The software company badly needed working capital in March, 1993, so it raised $3 million by selling 1.4 million shares to Irish investors at $2.10, a 30% discount to the U.S. price. While the firm's short position was normally no more than 25,000 shares, within days outstanding shorts soared to 981,000 shares. The share price fell 15% immediately, to $3, and at the end of the 40 days, most of the Irish shares came flooding into the U.S., further depressing the stock. "We were really ripped," says Phillip W. Smith, Zycad's CEO. The SEC is now investigating the trades.

That may give comfort to Smith. But most small companies that get burned have little recourse. Few have the cash to sue, and prosecutors often don't pursue cases. "When businesses are victims, it's hard to feel sorry for them," says Wayne Klein, former head of Idaho's Securities Bureau.

To help businesses avoid the sharks, several states have started seminars on financing for entrepreneurs. "We're here to tell companies they can be taken to the cleaners," says G. Philip Rutledge, director of Pennsylvania's division of corporate finance. The sad irony: Rutledge figures 20% of the attendees are unscrupulous promoters looking for their next pigeons.

By Michael Schroeder in Washington

AN OUNCE OF PREVENTION

Securities regulators say small businesses can avoid getting ripped off with a few precautions:

- Beware of promoters promising easy venture capital or business loans, particularly if they ask for up-front fees.
- Check references by getting written evaluations of a firm's service from former clients. Phone references may be accomplices.
- Check credentials with state securities or banking regulators. Be extra cautious if promoters are located in another state.
- Beware if someone wants to sell shares or reincorporate your company out of state, or do a large stock split. These hallmarks of the penny-stock scam are now being applied to small-cap stocks.
- Have a lawyer read the fine print of any agreement. Some contain fees that must be paid in cash, whether or not your company receives capital; others require signing over up to 10% of equity.

DATA: PENNSYLVANIA SECURITIES COMMISSION

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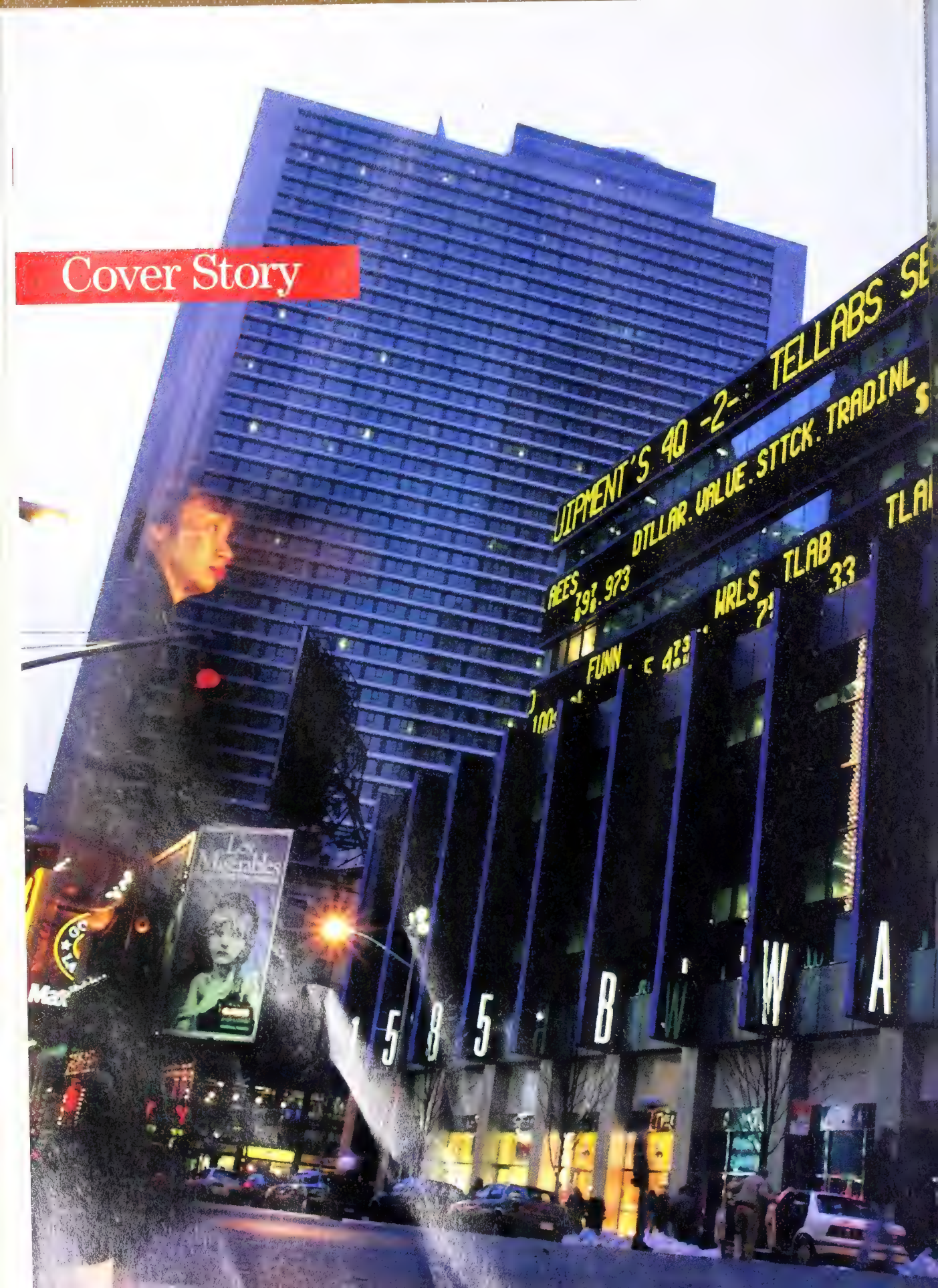
Cover Story



GLOBAL GAMBLE

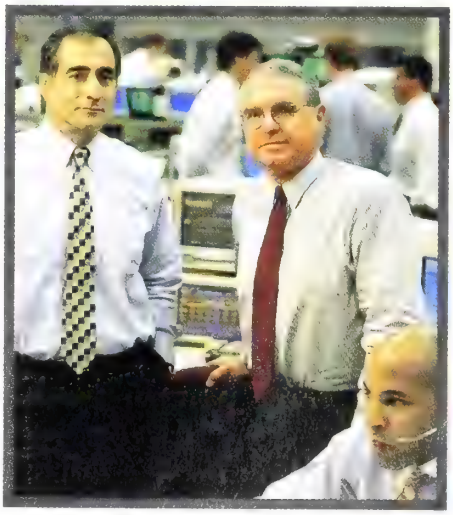
Morgan Stanley is charging into the Third World. Will it get burned?

The 90-year-old landmark building is anything but prepossessing—here in the Fort section of Bombay. The elevator is broken, forcing visitors to walk up the dilapidated stairs. But on the fourth floor is a modern office, with its own power and telecommunications lines and Indian employees working at computers. Welcome to fortress Morgan Stanley, a key beachhead on the subcontinent for the prestigious investment bank. Since 1992, Morgan Stanley Group has invested $25 million and recruited 62 employees, with plans to expand to 150 by 1998.

Despite India's ragged infrastructure—phones in this city of 14 million are unreliable, and the Bombay Stock Exchange is swamped by mountains of paper—Morgan Stanley is now the largest American investment bank in India. The firm's goal is to capitalize on the dramatic expansion of the Indian economy unleashed by extensive reforms. Morgan is convinced that it is getting in on the ground floor. "The advantage of being first is you can help shape things and events," says Pradip Darooka, executive vice-president of Morgan Stanley Trust Co.

India is far from the only place Morgan Stanley is planting its banner. The firm has been opening offices, raiding local talent, and scrambling for deals from Beijing to Johannesburg to São Paulo. Morgan is betting that the capitalist revolution sweeping through much of the world is irreversible and that newly minted free markets will generate red-hot economic growth and, eventually, profits. "High growth rates create wealth," says Richard B. Fisher, Morgan Stanley's chairman. "Wealth is what generates business for us."

SMALL TOWN. Leading the attack is Morgan Stanley's hard-charging president, John J. Mack. Lately, he has been skiing with Mexican clients, setting up a joint venture in Beijing, and angling for a role in the privatization of Indonesia's phone system in Jakarta. Mack, 51, hardly fits the mold for the quintessential white-shoe firm and lacks the pedigree one associates with Morgan Stanley. The son



CULTURE SHOCK AT HOME

ABOVE In their push overseas, Mack and Fisher are remaking the firm's white-shoe mold

LEFT Morgan Stanley's glitzy Times Square headquarters is wrapped in currency and stock quotes

(L TO R) PHOTOGRAPHS BY FREDERICK CHARLES

of Lebanese immigrants, he grew up in a small North Carolina town and worked throughout boyhood and college. A former bond trader, Mack is pushing Morgan Stanley to change its conservative culture, to become bolder and more aggressive. "It's grow or die," says Mack. "The biggest risk is not to invest."

Morgan Stanley's new Times Square headquarters symbolizes the transformation. It's an attention-getting glass box wrapped with neon bands of real-time currency quotes and stock prices. Inside is a high-tech hub of emerging-market information. Morgan Stanley staff have access from their desktop personal computers to an online database with exhaustive information on 65 countries. And Morgan Stanley Capital International, based in Geneva, creates and maintains 3,500 different international-market indexes that are the standard for the industry.

"MOST DARING." Morgan is not alone in betting on the Third World. It is waging a fierce battle with such U.S. archrivals as Merrill Lynch, Goldman Sachs, J.P. Morgan, and too many foreign banks and brokers to mention. Some are ahead of Morgan in certain markets, such as CS First Boston in Russia. Merrill Lynch has been lead manager of more large privatizations. But while it's hard to evaluate the extent of a firm's global presence, Morgan Stanley earns kudos for its all-around leadership position. "They are the premier emerging-markets firm," says J. Mark Mobius, president of Templeton Emerging Market Funds, a client and rival. "They are the broadest in scope and the most daring to move into new places, and they have a very large commitment."

NEW-MARKET GURU
Biggs popularized investing in emerging countries, so "you have to listen to him"

That commitment is driven by the need to develop new sources of high-margin business. In 1995 Morgan had a banner year, earning $600 million and ranking third in worldwide underwriting and first in U.S. and international mergers and acquisitions, says Securities Data Corp. But in the U.S., margins on such activities as underwriting are under extreme pressure. New markets are by nature more inefficient and thus more profitable than mature markets. Morgan Stanley is trying to repeat the success it had in Tokyo in the 1980s: Along with other U.S. securities firms, it reaped handsome profits with superior technology and sophisticated financial products.

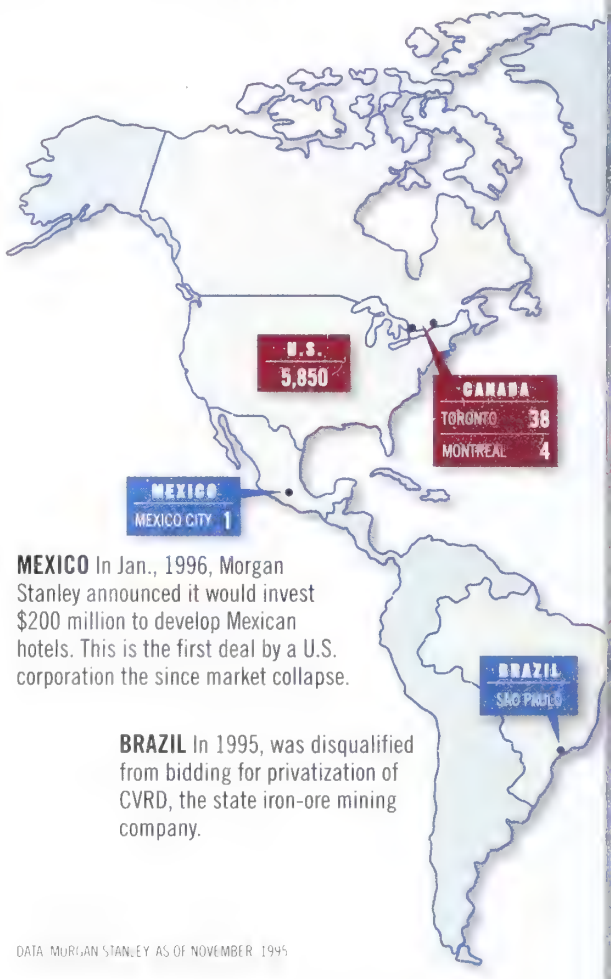
In the process, Morgan Stanley could emerge as an important architect of modern financial markets in countries such as India and China. As such, it would have considerable impact there. Morgan Stanley now acts as these nations' link to the world capital markets, which helps foster economic growth. For example, Morgan Stanley is pushing to set up a better system for clearing trades in Bombay and is building the first Chinese investment bank (page 68)—in much the same way it pioneered country funds, which brought long-term capital into developing countries.

Mack and Fisher are not betting the ranch. If Morgan Stanley's entire emerging-markets business dried up, the damage would be limited: It accounted for only 10%-15% of 1995 revenues, by one estimate. Morgan Stanley's strategy is to build for the long term in a focused, gradual, and cost-conscious manner. For instance, the firm opens an office only when a specific U.S. business unit, such as asset management or commodity trading, agrees to pay for its startup. Other businesses are then added gradually. In parts of the world where Morgan Stanley has no offices, it relies on frequent visits by bankers and analysts based in New York, Hong Kong, or London. "You can't look at it on a year-to-year basis," says Mack. "It's a marathon, not a race."

Nevertheless, Mack and Fisher are taking a big gamble with significant risks. Emerging markets are complex and treacherous. Most immediate is the financial impact. To build for the future, the firm is accepting lower earnings. Morgan's 17% growth in overseas personnel in 1994 cost the firm four percentage points in return on equity: Its ROE was 8.8%, instead of 12.8% in 1994.

TURBULENCE. The external risks are also huge. Business could dry up if U.S. pension, hedge, and mutual funds get cold feet about investing in emerging markets. When emerging-markets mutual funds fell 5% in 1995, many investors switched their investments to other funds. The firm itself could incur big trading losses in turbulent emerging markets, which it did in 1994. And there's the constant danger of political instability stalling market reforms. Many foreign financial markets are decades behind the U.S. and lack legal and regulatory protections, accounting systems, and clearing

Morgan Stanley's Wor

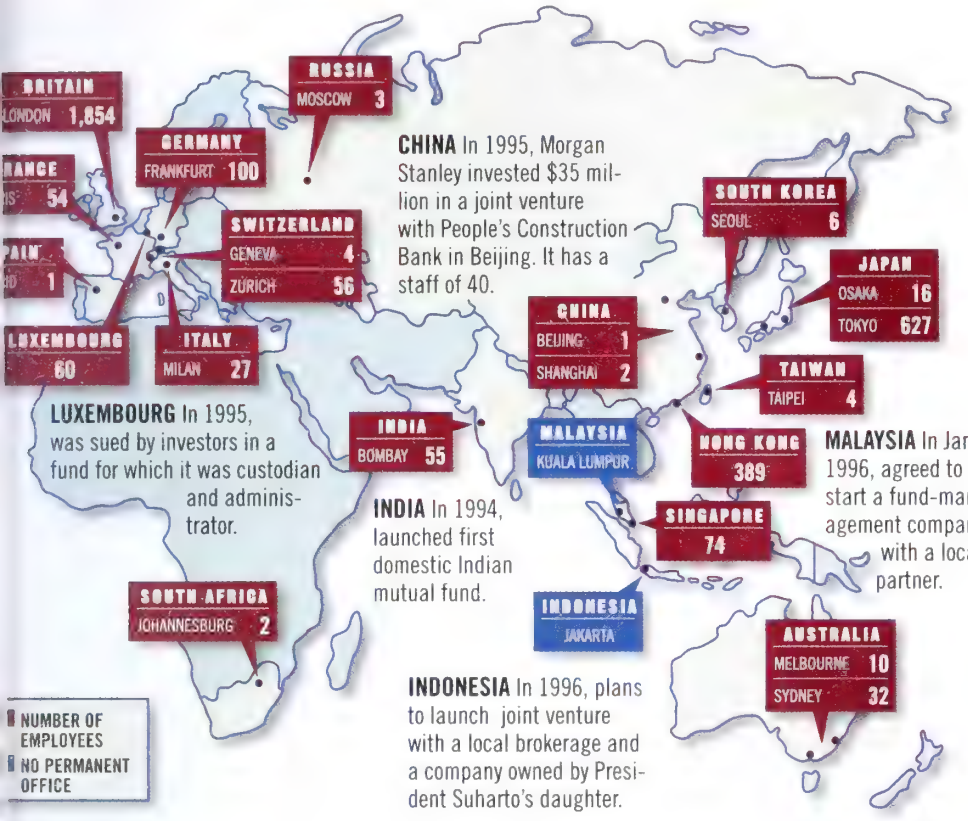


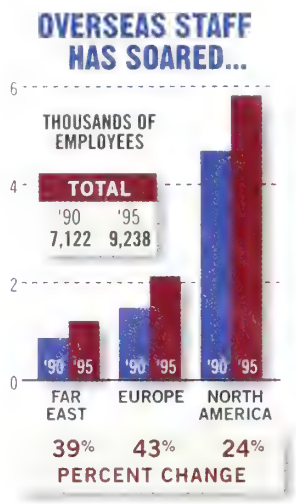
MEXICO In Jan., 1996, Morgan Stanley announced it would invest $200 million to develop Mexican hotels. This is the first deal by a U.S. corporation the since market collapse.

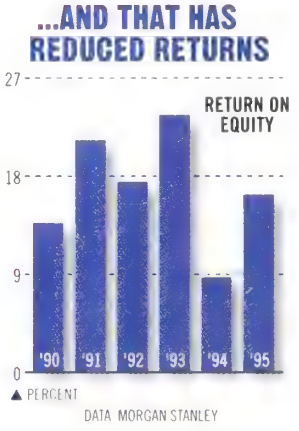
BRAZIL In 1995, was disqualified from bidding for privatization of CVRD, the state iron-ore mining company.

DATA: MORGAN STANLEY AS OF NOVEMBER 1995

ach The investment bank is scrambling to establish outposts around the globe. It has joint ventures in China, Indonesia, and Malaysia. And it is pursuing many types of business: privatizations, asset management, investment banking, global custody, and merchant banking.







echanisms. They can also be rife with fraud and corruption.

Perhaps Morgan Stanley's biggest risk is harm to its aunted reputation. In 1994, to loud fanfare, Morgan launched ndia's first mutual fund. But the launch was rocky, and the nd's performance mediocre. In 1995, the Bombay index fell .8% while the fund was down 28.2%. The effect was to tarsh Morgan Stanley's image in India (page 70). "Emerging arkets are very imprimatur-conscious, and Morgan Stanley a name they all understand," says Samuel B. Hayes III, a ofessor at the Harvard business school. "If they lose their od name, they're in trouble."

Fisher believes the risks are manageable. "We would not esitate to change course if the situation changed," he says. But everything we see as we get into these businesses conces us we're right."

Morgan Stanley has a history of transforming itself to lapt to change. The firm was formed in 1935, after the vernment forced commercial banks to shed their investment nking arms. Howard Stanley and Henry S. Morgan, son of P., resigned from J. P. Morgan & Co. and formed Morgan anley. Until the 1970s, Morgan Stanley was a private partrship. In the 1970s, it began a trading operation and by the e 1980s had built a major presence in London and Tokyo. ie firm went public in 1986. Yet Morgan Stanley is 40% emoyee-owned, and it retains its partnership culture.

The commitment to emerging markets comes right from e top. Fisher is the father of the firm's globalization push, t it took Mack's management muscle to break down fiefdoms within the firm to carry out the plan. Mack has worked for Fisher for his entire 21-year tenure at the firm, and the two are extremely close. While both visit clients, Mack runs the firm day-to-day, and Fisher concentrates on strategy. Fisher, 59, is a measured, private, Princeton man who is viewed as the firm's best salesman. "Dick makes you feel like you're the only person he has to see that day. There's a tremendous grace to that," says Robert Matschullat, ex-head of global investment banking at Morgan Stanley and now vice-chairman of Seagram Co.

By contrast, Mack is impatient, willing to trust his instincts, and runs a tight ship. Mack was furious when a budget for Morgan Stanley's Chinese joint venture, requested in August, 1995, hadn't been delivered by December. With the O. K. of his Chinese partners, he quickly replaced the head of the joint venture, Edwin Lim, even though Lim was the architect of the venture. "Running the bank was never really part of my assignment," Lim insists.

TIGHT SHIP. Mack is also known for bluntness. After moving to New York in 1968, he met broadcaster Charlie Rose and Rose's then wife, Mary, at a party. Mack's first question upon meeting Mary was, "Do you have a sister?" It turned out she had a sister named Christy, whom Mack later married.

Mack, the youngest of six boys, grew up in Mooresville, N. C. (pop. 11,000). His father ran a wholesale grocery business. Mack went to Duke University on a football scholarship and worked at a small brokerage—earning $325 a month.

Moving to New York, Mack took his first Wall Street job at

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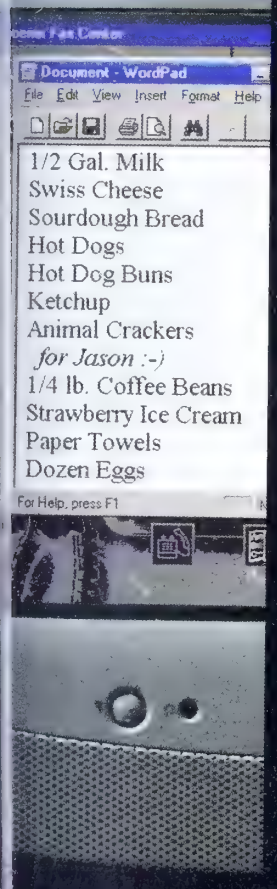

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Smith Barney, as a municipal bond trader and salesman. In 1972, Fisher, then head of fixed-income, hired him at Morgan Stanley. Mack made his name building Morgan Stanley's bond-trading operation, which became hugely profitable in the late 1980s. Mack earned respect as a tough, sometimes brutal manager. In 1993, he replaced investment banker Robert Greenhill as president.

Despite the $2.5 million Mack made in 1994 in salary and bonus, he remains down-to-earth. He lives in Westchester County, N.Y., with his wife and three children and has houses in North Carolina and Utah. His office is dominated by a large, realistic painting of a woman swimming underwater, and he keeps the TV on CNBC with the sound off. Mack enjoys hobnobbing with all types, from Senator Jesse Helms (R-N.C.) to Argentine President Carlos Menem to IBM CEO Louis V. Gerstner Jr. "For the head of a corporation, he doesn't surround himself with a lot of the trappings," says New York Police Commissioner William J. Bratton, a friend.

Morgan Stanley's push into emerging markets began in earnest when Mack became president. At the time, several rivals were cutting back. Mack decided this was just the mo ment to push hard. And he didn't want to repeat a 198 blunder: The firm cut staff in Hong Kong by 50 and deact vated its seat on the Hong Kong Stock Exchange, only t build back up in 1993. Competitors still love to remind client of Morgan's fickleness. "In 1989, we decided to take ou chips off the table in Hong Kong," says Mack. "We realized was a mistake."

Asia is clearly Morgan Stanley's top priority: From 1990 t 1995, the number of employees in Asia outside Japan soare from 90 to 540. Staff costs alone total $200 million a year.

INFLUENTIAL FRIENDS. A key to Morgan's success so far ha been its ability to adapt to local unwritten business rule which are infused by relationships and politics. A good ex ample is Morgan Stanley's campaign in Indonesia. Initially, th firm lost the 1994 competition to underwrite the privatizatio of PT Telkom, Indonesia's local phone system, to four othe Wall Street firms. Although Morgan said it could raise $2 bi lion, its rivals promised an impossibly large $3 billion. Th deal, which raised only $1.7 billion, was a fiasco.

Morgan Stanley had to settle for a secondary role—of f nancial adviser to PT Telkom—but it won points with gov ernment officials for giving more realistic advice. That helpe

IN BEIJING, THE LONG MARCH IS JUST STARTING

On the surface, things seem chaotic at China International Capital Corp. (CICC), Morgan Stanley & Co.'s pioneering, six-month-old joint venture with People's Construction Bank and several other partners. In December, 1995, Edwin Lim, a former World Bank director who engineered the $100 million deal, was pushed out as chief executive of CICC by Morgan Stanley and replaced by his subordinate, Harrison Young.

Young, whose Chinese is rusty, says Chinese and Western executives at CICC's office in Beijing often have to communicate through bilingual secretaries. And tenfold pay discrepancies between bankers with international experience—both Americans and Chinese—and bankers who have only worked in China are causing motivational problems. "The biggest challenges we face are cultural," says non-English-speaking Tang Shisheng. He and Fang Fenglei are CICC's deputy chief executives.

LEAPFROG. Despite these difficulties, CICC holds a long-term promise of enormous opportunity for Morgan Stanley, a relative latecomer to China. CICC, the firm's largest single investment in an emerging market, is the only Chinese investment bank with a foreign partner licensed to do business in China. Beijing views CICC as a way to build a Chinese Morgan Stanley. Morgan Stanley, for its part, sees CICC as a way to become a major player in China's domestic capital market, which is off limits to its rivals. And Morgan is betting that CICC will help it leapfrog earlier arrivals—such as Merrill Lynch and CS First Boston—in getting China's international business.

LANGUAGE HURDLE

To communicate, Tang, Young, and Fang often rely on bilingual secretaries

Even these contenders acknowledge that CICC is a daring gamble, like any other joint venture in China. "We all thought CICC was very brave," says a major rival. Says another: "If they hang in there, I expect they'll be rewarded down the road. The Chinese are the kind of people who appreciate something like this being done at a time when everyone else was leaving."

IN A SLUMP. It may be years, though, before the 40-person CICC gets a return on Morgan Stanley's $35 million investment. Meanwhile, business deals seem to be going to Morgan Stanley's competitors. Merrill Lynch & Co. has just floated the first $400 million China Yankee bond deal.

Still, the unique combination of Morgan Stanley's skill and Chinese connections is producing some business, even though China's capital markets are in a slump. CICC is helping Jilin Oil search for an investor in the company's oil field. And CICC is holding discussions with several foreign corporations about finding local partners. Says John S. Wadsworth Jr., chairman of Morgan Stanley Asia Ltd.: "Things are about where we expected them to be." Pioneering in China isn't for the faint-hearted, and CICC could be the supreme test of Morgan's global strategy.

By Dave Lindorff in Hong Kong

Morgan proceed with a longstanding plan to set up a joint venture with two well-connected, local partners. The partners are a holding company owned by Siti Hardiyanti Rukmana, a daughter of President Suharto, who has held power for three decades, and PT Makindo, an Indonesian brokerage. The venture will be capitalized at $10 million and should be up and running this year. If all goes well, Morgan Stanley will underwrite lucrative initial public offerings as the government gears up to privatize 50 of the companies it owns.

ASIA PULP & PAPER

In seeking such Indonesian clients, Morgan Stanley will rely on its ties to Suharto's family

Morgan is also gaining entrée to developing countries by using its established global businesses. Take Morgan Stanley Asset Management (MSAM), which manages $100 billion. Morgan is a top manager of institutional and retail emerging-markets funds: Its only serious Wall Street competitor is Merrill Lynch. In emerging-markets assets, it ranks fourth—after Templeton, Fidelity, and Capital Guardian—with $5.2 billion. In Thailand and Indonesia, being in early with country funds gave Morgan an edge in winning investment-banking deals. "Our presence through MSAM in traded financial markets is clearly the most important advantage we have," says Fisher.

LOQUACIOUS. MSAM's chairman is Barton Biggs, who played a key role in giving Morgan Stanley a headstart in emerging markets. Biggs worked with International Finance Corp., an arm of the World Bank, in the mid-1980s to get Morgan Stanley to launch some of the first country funds, such as the Malaysia Fund in 1985. Some of Biggs's calls have been wrong, and others have landed the firm in hot water with local authorities. Yet the persuasive Biggs gets credit for popularizing investing in emerging markets. For years, he has been promoting such remote places as Myanmar and Vietnam. He has a following among a group of influential U.S. and foreign institutional investors who accompany him on his annual trip to different emerging markets. "He moves markets, so you have to listen to him," says one money manager.

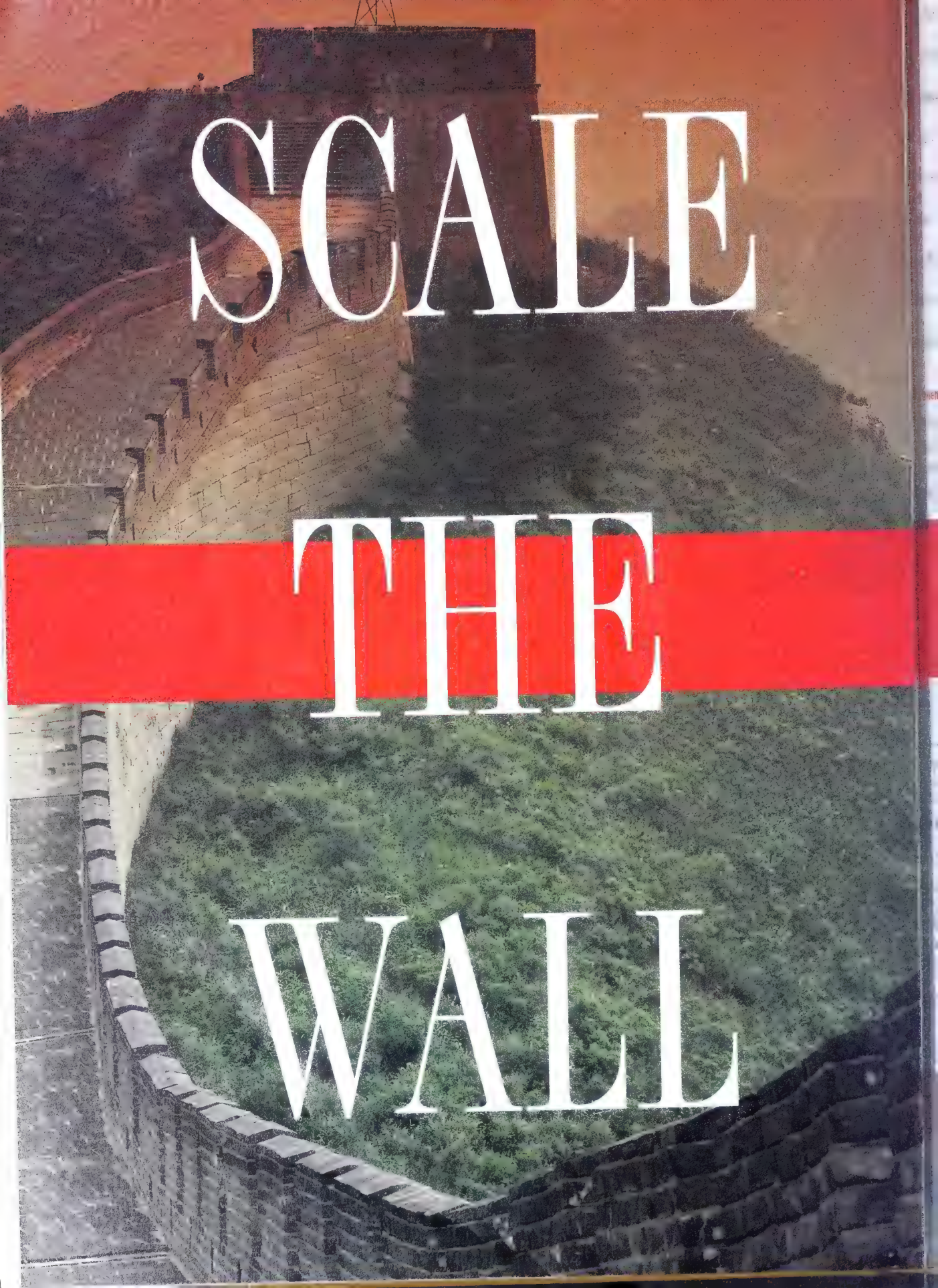
MSAM is not the only unit that gives Morgan Stanley great on-the-ground intelligence on emerging markets. Morgan Stanley Capital Partners, the firm's merchant-banking fund, has $100 million invested in three Chinese and Indonesian firms. Its global custody business, the mundane business of clearing and settling trades for clients in 64 countries, provides Morgan with an intimate familiarity with the nuts and bolts of each nation's markets. Morgan Stanley is the only U.S. investment bank in this business, where it competes with U.S. commercial banks. It ranks 11th, with $117 billion worth of assets in custody. Morgan Stanley executes trades through a worldwide network of banks and a sophisticated computer system.

HIGH HURDLES. Will Morgan Stanley's global bet pay off? The firm has done a solid job entrenching itself around the world, but it faces many hurdles because of primitive financial infrastructures in many countries. In Russia, for example, stockholders don't legally own stock until their names are written on a list maintained by the companies' registrar. This means that to process trades, Morgan agents must travel to the registrars to make sure the names are on the lists. In India, it takes 12 days for a trade to clear, and a stack of paper a foot high is generated to clear one trade.

The firm must deal with cultural challenges as well. Some 34% of its employees are locals in their respective countries—and they span 20 different nationalities. This makes it more difficult to maintain high standards and its cohesive WASP culture, which dictates even where headquarters staff should live, namely, Greenwich, Conn., or Rye, N.Y. "We have to work hard to demonstrate we're not a bunch of white guys from Greenwich," says Thomas DeLong, Morgan Stanley's chief development officer.

More serious, though, is its vulnerability to well-heeled rivals. For example, in December, 1995, it lost to Merrill Lynch in vying for the job of selling Brazilian mining giant Companhía Vale do Rio Doce (CVRD)—likely to be Latin America's largest privatization ever. One miscue was Morgan's bidding strategy: It went from a front-runner to being disqualified because its bid was too low even to be considered.

But that was only part of the problem. Morgan Stanley has strong Latin American credentials, with its team led by Francisco Gros, former president of the central bank of Brazil. He and other Morgan bankers and analysts in New York frequently visit Latin American clients. But Merrill Lynch, which won the $5 billion CVRD mandate and could take in the bulk of a juicy $95 million fee, has nearly 100 employees in Brazil and is highly visible in local financial circles. Rivals say Morgan lost because it lacks local presence and experience. "Your level of understanding is different when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you're here," says Eduardo Saad, managing director of Merrill Lynch in São Paulo.

Morgan Stanley faces tough competition from commercial banks with investment-banking capabilities. In 1994, for example, Morgan Stanley won over 40% of all Mexico's equity issues. But in December, 1994, when the new government devalued the peso and plunged the country into recession, Morgan Stanley's business dried up overnight. Mexican company stocks plummeted, and the international markets snapped shut.

But commercial banks with investment banking arms as well, particularly J. P. Morgan and CS First Boston, were able to offer corporate clients emergency bridge loans during the crisis, a capability Morgan just announced in January, 1996. Grateful clients rewarded those banks with their first international debt issues when capital markets reopened six months later. "The banks that wear two hats [investment and commercial] are in a particularly advantageous position in Mexico today," says Peter T. Hutchison, who was chief financial officer of Grupo Alfa, a Monterrey conglomerate. Even the recent privatization plums have gone elsewhere: J. P. Morgan is advising the government on the petrochemical sell-off, and CS First Boston beat out Morgan for the government contract for the railroads.

With so many businesses, Morgan Stanley must be careful about potential conflicts between its own and its customers' interests. In Europe, Morgan Stanley is fighting accusations about its conflicting roles in the collapse last year of the $120 million Global Opportunity Fund, registered in the Cayman Islands. Morgan Stanley's Luxembourg operation was the fund's custodian and administrator. While Morgan's London office lent $34 million to the fund's investors, 20 investors claimed losses of $70 million and are suing the firm in a Luxembourg court for gross negligence, mainly over Morgan Stanley's inflated valuations of the fund. Investors also say that when the fund tanked, Morgan Stanley's first priority was to recover the $34 million. A firm spokesperson denies this and blames the collapse on the fund manager, saying he misled them on the fund's value and made unauthorized trades.

Given the hazards of the markets in which it is playing, Morgan Stanley could well stumble as often as it succeeds. It believes, though, that it is taking intelligent, cost-conscious risks. "I think we have the most resources and the most conviction," says Fisher. "We could be wrong. We won't know for five years whether we are right."

By Leah Nathans Spiro in New York, with Sharon Moshavi in Bombay, Michael Shari in Jakarta, Ian Katz in São Paulo, Heidi Dawley in London, Geri Smith in Mexico City, and Dave Lindorff in Hong Kong

A SPRINT TURNS INTO A STUMBLE

In April, 1994, Morgan Stanley & Co. became the first foreign company to launch a domestic mutual fund for retail customers in India. It looked as if the fund was going to be a smash hit.

Awed by the company's reputation, Indian investors lined up in droves. Over the course of 2½ days, 1.5 million people turned $310 million over to Morgan Stanley. That's when the trouble started. Investors, who said that the firm had promised there would be a $100 million ceiling, complained the fund was less exclusive than they had been led to believe. Morgan Stanley executives say its prospectus had clearly stated the fund had no maximum limit.

TATTERED REPUTATION. Then, before the fund's shares were listed on the Bombay Stock Exchange, the units started trading illegally—at 89¢ each instead of the initial price of 32¢. But when the fund hit the market, the units crashed—to 19¢ apiece. Since the launch, the fund's performance has been lackluster: Since 1994, the fund has declined 16.5%, compared with a 17.7% drop for the Bombay index. Morgan Stanley was not accused of wrongdoing in the ensuing investigation into the gray market trading, but its sterling reputation was in tatters and still hasn't fully rebounded. "When Morgan Stanley first came, people were fascinated. Now, they are very disappointed," says Prem Advani, an independent investment agent in New Delhi.

BANKER KIDWAI

Morgan Stanley's perspective is "long-term"—after its rocky start in India

Morgan Stanley says the main problem is that Indian investors didn't understand mutual funds. "People thought they were buying a Morgan Stanley share, not an emerging-market fund," says K. N. Vaidyanathan, vice-president of Morgan Stanley Asset Management India Private Ltd.

Barry Hall, a former Peace Corps volunteer who heads Morgan Stanley's India office, acknowledges that this has "led to a long-term PR problem." Other observers say Morgan Stanley doesn't appreciate the nuances of the Indian market. Says Sanjeev Mohta, head of research at James Capel B&K in Bombay: "You cannot necessarily use global or even Asian parameters to understand things here."

Morgan Stanley also is viewed with a bit of suspicion because it has become so big in the Indian market. Its asset-management portfolio of $1.6 billion is 1.25% of the capitalization of the Bombay market, and it represents about 7% of trading volume. That makes the firm the largest owner of Indian stocks after Unit Trust of India, the government-run mutual-fund operator. Some Indian traders say Morgan could move the market, and that makes people nervous.

Morgan Stanley officials say they will continue to expand their many businesses in India. "Only a few firms can afford to take a long-term perspective," says Naina Lal Kidwai, Morgan Stanley's investment banking chief in Bombay. By forging ahead, Morgan Stanley is proving it won't be discouraged by one setback.

By Sharon Moshavi in Bombay

BY GENE G. MARCIAL

IS GM THE ONE TAILGATING AMEX?

There may be a big G in the future for American Express.

When this column pointed out that American Express (AXP) was undervalued and was perhaps being stalked by a huge financial-services outfit (BW—Feb. 5), some analysts identified the rumored stalker as General Electric. GE instantly issued a denial. But now, there may be another suitor—whose name also starts with a big G: General Motors.

"The story about AmEx as a buyout target is far from over, in spite of the GE statement" says one investment banker who has been right on the mark in spotting takeovers. He isn't discounting GE as a contender but says GM, with its huge excess cash flow and global reach, has the wherewithal and strategic motives to pursue AmEx.

He says GM's General Motors Acceptance Corp., which serves customers' financing and insurance needs, would benefit from AmEx' banking, insurance, and credit-card operations. GM started a credit-card program in 1992. He adds: 'My contact close to the GMAC people tells me that some GM bigwigs are very interested in AmEx."

This banker says GM produces excess cash flow of more than $4 billion a year. Apart from GMAC, GM owns Electronic Data Systems and Hughes Electronics. EDS and GM Hughes trade separately on the New York Stock Exchange: GM's Class E stock represents EDS, and Class H is GM Hughes.

Some observers put the takeover value of AmEx, now trading at 44, at 60 a share—or $30 billion in total. GM spokesman Mark Tanner says corporate policy is not to comment on any future acquisitions. AmEx didn't return calls.

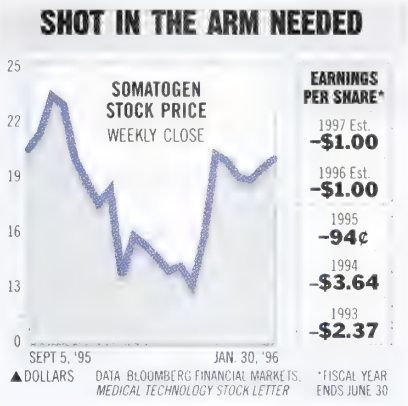
FOR SOMATOGEN, IT'S IN THE BLOOD

If investment adviser Jim McCamant is right—as he was about Amgen and Chiron a decade ago—Somatogen (SMTG) is the next biotech to catch. He discovered Chiron in 1984, when it was at 4%. It's now at 112. He found Amgen in 1985, when it was at about 50¢ (adjusted for splits). Amgen is now at 69.

McCamant, editor of the *Medical Technology Stock Letter* in Berkeley, Calif., sees Somatogen as "the next Amgen-Chiron." The leader in developing a genetically engineered red-blood-cell substitute, "Somatogen in five years will have the largest-selling product in that potentially huge market," says McCamant. He thinks the stock, now at 19, will hit 50 in a year.

Somatogen hasn't been a wallflower: It went public in January, 1991, at 19—and zoomed to 50 by January, 1992. When the biotech bloom faded, so did Somatogen, slumping to 8 by March, 1993. The stock revived when the company took its chief blood-substitute product, Optro, to clinical trials.

In 1994, Eli Lilly signed a pact with Somatogen, investing about $30 million



so far and taking a 5% stake, to develop Optro. Lilly will produce Optro and has exclusive world rights, except for North America and Scandinavia.

This year, Lilly and Somatogen plan to start an expanded trial of Optro for blood loss during surgery. McCamant thinks Optro will be commercially launched by 1998. One advantage of substitute blood cells is that blood typing isn't necessary. And there is no danger of getting blood-borne diseases. Also, donated blood keeps for only 35 to 42 days and must be refrigerated.

McCAMANT: *Ace picks in biotech*

Analysts note that more than 12 million units of red-blood cells are transfused in the U.S. every year. At $200 a unit, that's a $2.5 billion market.

Analysts figure Lilly can make 800,000 units a year. Other companies, such as Baxter Laboratories, are also developing blood substitutes. But Somatogen, says McCamant, seems to have a cost advantage and, through its partnership with Lilly, the resources to meet heavy demand.

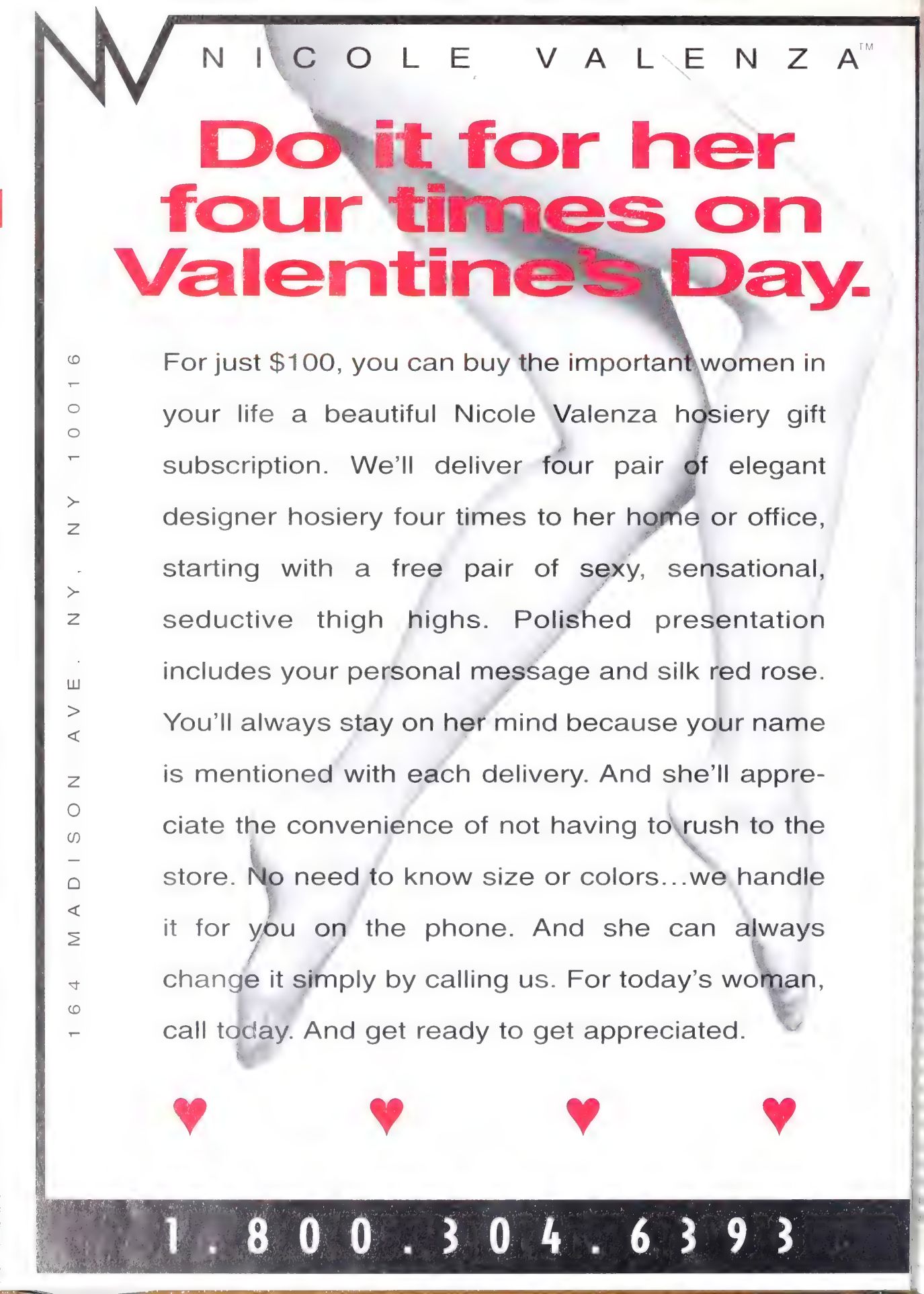
HORIZON'S VIEW MAY BE TOO ROSY

One quick route to growth is acquisitions, and Wall Street loves Horizon/CMS Healthcare (HHC) for it. The company has been on a fast track with its recent deals. As a result, Horizon's shares are buoyant, rising to 26 from 18 in late October. But not everyone is pleased: Howard Schilit and Debbie Meritz of the Center for Financial Research & Analysis in Rockville, Md., contend that Horizon, which operates long-term-care facilities in 18 states, "overstated its operating income and engaged in aggressive accounting" when it acquired Greenery Rehabilitation Group in February, 1994, and Continental Medical Systems in July, 1995.

Meritz believes Continental Medical's "revenue may have been overstated" in periods prior to being acquired. In the three years before the deal, says Meritz, Continental recorded special charges to write off costs and assets that could have been expensed in future periods. The charges indicated to Schilit and Meritz that Continental used aggressive accounting by capitalizing costs on its balance sheet.

Horizon itself, notes Meritz, took large special charges: In the first quarter of fiscal 1996, Horizon posted a $63.5 million charge, enabling the company to avoid future expenses while setting the stage for impressive earnings growth later. Included in the write-offs, notes Meritz, are future bonus rights to Horizon's vice-chairman and pre-opening costs that could be expensed soon.

The effect of writing off costs as a special charge is to exclude normal operating costs from operating income and to shift future costs to the current period. So earnings get a boost in the periods in which these costs were written off. She says reported earnings of $1.03 for the year ended May 31 would have been lower had they not taken those charges. Horizon's CFO Michael Seeliger rejected the claim that the company engaged in aggressive accounting. "We follow accounting principles and our auditors reviewed our financials and gave comfort on everything that we did."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BOND FUNDS CAME BACK. WILL INVESTORS?

quities are getting all the attention, but bonds hold plenty of potential for gains

Suppose the bond market staged a rally and nobody came. That's what happened during 1995. Bond mutual funds scored solid double-git total returns of 16.4%, including vidends and capital-gains distributions, ore than reversing 1994's losses. That asn't enough to keep investors in the ld, as $4 billion more flowed out of e funds than went in, a striking con-ast to the $129 billion that piled into quity funds. This year, about $2.6 bil-n has come back to bond funds, but vestors are deploying it very selec-vely, according to AMG Data Services, hich tracks flows to funds. Most of e new money is going to corporate nd funds. Municipal bond funds are t, and money is still exiting the gov-nment bond funds.

Perhaps some prospective investors ere scared off by the 1994 bear market and didn't believe—along with most of the pros—that bonds would come roaring back. And others no doubt found the lure of a rising Dow irresistible and ran to equity funds instead. Now, having missed the tremendous capital gains, there's not much incentive to move back to bond funds. While long-term rates dropped two percentage points, short-term rates have fallen only a half percentage point. So yield-sensitive investors are sticking with money-market funds rather than exposing themselves to the volatility of longer-term bond funds.

RATING RISK. But in avoiding bond funds, investors are also forgoing the opportunity to earn capital gains that sometimes dwarf yields. It's total return, not yield, that counts in measuring your investment returns. And that's what you'll find in the BUSINESS WEEK Mutual Fund Scoreboard, which this week reports on 652 bond funds. In the tables, prepared by mutual-fund data company Morningstar Inc., we report total returns over the past one-, three- and five-year periods. We also examine yield, maturity, and a fund's performance relative to other funds, and we report on the fees and expenses. The lower the cost of the fund, the more that's left for investors—and that counts for a lot in a low-yield world.

Even total return does not tell the whole story. The Scoreboard rates funds based on their risk-adjusted total returns over the past five years and awards them anywhere from three upward-pointing arrows, meaning superior performance, to three downward-pointing arrows, for the poorest showings. This year, 39 bond funds earned top honors (table).

The list would put a big smile on the

The Top Performers

These 39 bond funds have earned three upward-pointing arrows in the BUSINESS WEEK Mutual Fund Scoreboard. To get this rating, they needed to deliver superior risk-adjusted total returns over the last five years.

FUND	AVERAGE ANNUAL TOTAL RETURN*	INVESTMENT OBJECTIVE
AIM HIGH-YIELD A	18.1%	Corporate–High-yield
CALVERT TAX-FREE RESERVES LTD.-TERM A	4.7	Municipal–National
COLONIAL HIGH-YIELD SECURITIES A	19.6	Corporate–High-yield
DAVIS TAX-FREE HIGH INCOME B	7.7	Municipal–National
DEAN WITTER HIGH-YIELD SECURITIES	24.3	Corporate–High-yield
DELAWARE TAX-FREE USA A	8.7	Municipal–National
DREYFUS SHORT-INTERMEDIATE MUNICIPAL BOND	5.6	Municipal–National
FEDERATED HIGH-YIELD	18.9	Corporate–High-yield
FIDELITY ADVISOR HIGH-YIELD A	18.5	Corporate–High-yield
FIDELITY CAPITAL & INCOME	18.3	Corporate–High-yield
FIDELITY SPARTAN HIGH-INCOME	19.2	Corporate–High-yield
FIDELITY SPARTAN SHORT-INTERMEDIATE MUNI	6.1	Municipal–National
FIRST INVESTORS FUND FOR INCOME A	18.6	Corporate–High-yield
FLAGSHIP LIMITED-TERM TAX-EXEMPT A	7.1	Municipal–National
FRANKLIN AGE HIGH INCOME I	18.9	Corporate–High-yield
FRANKLIN HIGH YIELD TAX-FREE INCOME I	9.5	Municipal–National
FRANKLIN PA TAX-FREE INCOME I	9.0	Municipal–Single-state
KEMPER DIVERSIFIED INCOME A	20.0	Multi-sector bond
KEMPER HIGH-YIELD A	19.0	Corporate–High-yield
LIBERTY HIGH-INCOME BOND A	20.9	Corporate–High-yield
MAINSTAY HI-YIELD CORPORATE BOND B	18.9%	Corporate–High-yield
MERRILL LYNCH CORPORATE HIGH-INCOME B	17.0	Corporate–High-yield
MFS HIGH-INCOME A	18.9	Corporate–High-yield
MFS MUNICIPAL HIGH-INCOME A	8.1	Municipal–National
NORTHSTAR ADVANTAGE HIGH-YIELD T	19.8	Corporate–High-yield
NUVEEN MUNICIPAL BOND R	8.1	Municipal–National
T. ROWE PRICE TAX-FREE HIGH-YIELD	9.0	Municipal–National
T. ROWE PRICE TAX-FREE SHORT-INTERM.	5.7	Municipal–National
PUTNAM HIGH YIELD ADVANTAGE A	18.7	Corporate–High-yield
PUTNAM NY TAX EXEMPT OPPORTUNITIES A	8.3	Municipal–New York
SELIGMAN HIGH-YIELD BOND A	17.9	Corporate–High-yield
SIT TAX-FREE INCOME	7.8	Municipal–National
SMITH BARNEY MUNICIPAL LIMITED-TERM A	7.2	Municipal–National
THORNBURG LIMITED-TERM MUNI. NATIONAL A	6.6	Municipal–National
UNITED MUNICIPAL HIGH-INCOME A	9.6	Municipal–National
USAA TAX-EXEMPT SHORT-TERM	5.6	Municipal–National
VAN KAMPEN AMERICAN CAP. HIGH-YIELD MUNI A	8.7	Municipal–National
VANGUARD MUNICIPAL BOND LIMITED-TERM	6.1	Municipal–National
VANGUARD MUNICIPAL BOND SHORT-TERM	4.7	Municipal–National

*Pretax return, appreciation plus reinvestment of dividends and capital gains, 1991–95

DATA: MORNINGSTAR INC.

High-yield corporate and high-yield muni bond funds dominate the Scoreboard's list of top performers

face of Michael R. Milken, the onetime junk-bond king of Wall Street. Seventeen of the funds are high-yield corporate bond funds, which invest in bonds rated below investment grade—the sort of securities he popularized in the 1980s. The theory behind junk bonds is that while there's greater risk of default, higher yields more than make up for occasional bad bonds.

Many of the top-rated tax-free funds are also high yielders. But with municipal bond funds, it's more unrated debt than low-rated debt that provides the extra juice. In the diffuse and inefficient muni market, funds with the ability to perform their own research often find creditworthy investments among smaller issuers who find it cheaper to pay a somewhat higher interest rate on their bonds than to pay for a debt rating from a ratings agency.

What's also noteworthy about the top performers list is what's not on it: a government bond fund. That's got nothing to do with the furious budget battle or the fear of a default. In fact, no government bond funds even merited two up arrows, the second-highest rating, and only a handful come up with better-than-average marks. One reason for this poor showing was that the devastating 1994 bond market hit government debt the hardest, lowering returns and raising risk ratings.

But even without 1994, government bond funds are not compelling. In the corporate or muni markets, smart credit research and good portfolio management can pay off. But in the government market, the most efficient securities market in the world, there are few inefficiencies to uncover and little value added by fund managers, especially after taking into account sales charges and ongoing fund expenses.

Before you rush to high-yield funds, remember that you're viewing them under near ideal conditions. Over the past five years, the period for the 1996 ratings, junk bonds have had the wind at their backs. Interest rates fell, allowing many issuers to refinance; corporate cash flows swelled, improving issuers' ability to service their debt; and the economy, though slow at times, grew and stayed clear of recession.

DEFENSE. Keep in mind, too, that junk funds earned high marks because their 1989-90 bear market is no longer in the the ratings period. The best example of a fund that benefits from the turn of the calendar is Dean Witter High-Yield Securities, with 24.3% average annual total return. In 1990, the fund had a horrendous -40.1% return. Its standout five-year record was launched in 1991, when the market rebounded and the fund amassed a 67.2% return. The fund also beat the competition in 1992 and 1993, but has been a laggard since.

Managers of the top-rated high-yield funds acknowledge that things have gone well since 1991 and are mindful that things might not always be so bright. "We've turned defensive," says Robert J. Manning, who runs MFS High-Income A fund. Manning has upgraded the portfolio to larger, more established issuers and has moved away from sul ordinated to more senior debt.

But Mark E. Durbiano, who rur both Federated High-Yield Fund ar Liberty High-Income Bond A Fun takes a different view. He does n think the economy will slow enough derail the high-yield market. In add tion, he says the spread between jun bond yields and Treasury yields is mo than 4 percentage points, the wide gap since November, 1993. That yie advantage should lure new money in the market. Says Durbiano: "The hig yield outlook for 19 is pretty bright."

With munis, t main worry is not i terest rates or cred quality but the pro pects for replacing t graduated income ta with a one-rate "fl tax." Under a pla whose chief proponen include House Major ty Leader Richard Armey (R-Tex.) ar Republican Presidenti hopeful Malcolm Forbes Jr., the ta preference for mun would end as all i vestment income b came tax free. In th case, muni prices wou fall until their yiel approximated those government and corp rate bonds.

Indeed, muni bon are already cheap r ative to taxables. If t flat-tax threat subsides, munis and mu bond funds should rally. Sheila Amoros who runs the top-rated Franklin Hi Yield Tax-Free Income I, says the fl tax has no fizz because it would scr popular deductions for interest on hor mortgages and state and local taxe "It's like health-care reform," she say "It sounds great on the surface, b start scratching away at the details a it will become extremely unpopular."

Thinking about investing in mu funds? Or any other bond funds for th matter? Your bond-fund search sta with the Scoreboard on page 77.

By Jeffrey M. Laderma in New Yo

The Bond-Fund Rebound

Interest rates fell, so most bond funds earned double-digit returns in 1995. The damage from a disastrous 1994 is evident in the three-year returns, which are weaker than the one- or five-year numbers.

FUND OBJECTIVE	AVERAGE ANNUAL TOTAL RETURN* 1995	1993–95	1991–95	BEST PERFORMER IN 1995
CONVERTIBLE	22.6%	11.8%	16.4%	Bond Fund for Growth A
GOVT.—TREASURY	22.2	9.0	10.2	Benham Target Maturities 2020
CORP.—GENERAL	18.3	8.4	10.3	Smith Barney Inv. Grade Bond B
MUNI.—CALIFORNIA	17.8	7.3	8.3	Alliance Muni. Inc. Ins. CA A
MULTI-SECTOR BOND	17.8	8.8	12.3	AIM Income A
CORP.—HIGH-YIELD	16.9	10.5	16.9	IDS Extra Income A
WORLD BOND	16.8	8.3	8.1	Alliance N. Amer. Govt. B
MUNI.—NEW YORK	16.6	6.8	8.6	Lebenthal NY Municipal Bond
MUNI.—SINGLE-STATE	16.2	7.1	8.4	Voyageur FL Insured Tax-Free A
GOVT.—MORTGAGE	15.9	6.5	8.0	Princor Govt. Secs. Income A
CORP.—HIGH-QUALITY	15.9	7.2	8.8	Vanguard F/I L/T Corp. Bond
MUNI.—NATIONAL	15.5	7.0	8.2	Alliance Muni. Inc. Ins. Natl. A
GOVT.—GENERAL	15.4	6.3	7.8	Fidelity Spartan L-T Govt.
S-T WORLD-INCOME	9.0	3.4	3.3	TCW/DW N. Amer. Govt. Inc.
GOVT.—ADJ. RATE MTGE.	8.2	4.0	4.9	Franklin Adj. U.S. Gov. Secs.
ALL BOND FUNDS	16.4	7.4	9.3	*Pretax return, includes reinvestment of dividends and capital gains
TAXABLE FUNDS	16.6	7.8	10.4	
TAX-FREE FUNDS	16.3	7.1	8.5	DATA: MORNINGSTAR INC

MUTUAL FUND SCOREBOARD

ow to Use the Tables

ISINESS WEEK RATING
tings measure risk-adjusted rformance. This shows how ll a fund performed relative to ıer funds and relative to the el of risk it took. Risk-adjusted rformance is determined by ɔtracting a fund's risk-of-loss :tor (see below) from its his-ic total return. Performance culations are based on the e-year time period between ı. 1, 1991, and Dec. 31, 95. For rating purposes, funds : divided into two groups: ınicipal bond funds and all ıer funds. Ratings are based a normal statistical distribu-n within each group and arded as follows:

- ♦ ♦ SUPERIOR
- ♦ VERY GOOD
- GOOD
- AVERAGE
- BELOW AVERAGE
- ♦ POOR
- ♦ ♦ VERY POOR

RISK
The risk-of-loss factor is the potential for losing money in a fund, calculated as follows: The monthly Treasury bill return is subtracted from the fund's total return for each of the 60 months in the rating period. When a fund has not performed as well as Treasury bills, the result is negative. The sum of these negative numbers is then divided by the number of months in the period. The result is a negative number, and the greater its magnitude, the higher a shareholder's risk of loss.

PERFORMANCE COMPARISON
The tables provide performance data over three time periods. Here are equivalent total returns for the Lehman Brothers bond indexes during those periods:

	GOVT./CORP.	MUNI.
1995	19.2%	17.5%
3-year average (1993-95)	8.5%	7.8%
5-year average (1991-95)	9.8%	8.8%

FUND CATEGORIES
Corporate, Government, Municipal, International, and Convertible.

SALES CHARGE
The cost of buying a fund, commonly called the "load." Many funds take loads out of initial investments, and for ratings purposes, performance is reduced by these charges. Loads on withdrawals can take two forms. Deferred charges decrease over time. Redemption fees are imposed whenever investors sell shares. Funds with none of these charges are called "no-load."

EXPENSE RATIO
Fund expenses for 1995 as a percentage of average net assets. The measures show how much shareholders pay for fund management. Footnotes indicate 12(b)-1 plans, which allocate shareholder money for marketing costs. The average expense ratio is 1.01% for taxable funds, 0.84% for tax-free funds.

TOTAL RETURN
A fund's net gain to investors, including reinvestment of dividends and capital gains at month-end prices.

YIELD
Income distributions during 1995 expressed as a percent of net asset value, adjusted for capital gains.

MATURITY
The average maturity of the securities in a fund's portfolio, weighted by market value.

TREND
A fund's relative performance during the five 12-month periods from Jan. 1, 1991, to Dec. 31, 1995. The boxes read from left to right, and the level of green in each box tells how the fund performed relative to other funds during the period: for the top quartile; for the second quartile; for the third quartile; and for the bottom quartile. An empty box indicates that a fund is not rated for that time period.

TELEPHONE NUMBERS
See index on page 87.

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
						TOTAL RETURN (%)					
		ASSETS $MIL.	% CHG. 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	1 YR.	3 YR.	5 YR.	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
CORPORATE											
ARP HIGH-QUALITY BOND	♦	544.8	3	No load	0.95	17.3	7.5	8.8	5.7	11.5	
DVANCE CAPITAL I RETIREMENT INCOME		139.3	64	No load	0.88†	23.0	9.9		7.2	17.4	
IM HIGH-YIELD A	♦♦♦	880.7	53	4.75	1.00†	16.9	10.8	18.1	10.1	8.1	
IM INCOME A	♦	249.7	25	4.75	0.98†	22.8	9.4	10.6	7.5	14.6	
LLIANCE BOND CORPORATE BOND B		299.4	44	3.00**	1.99†	27.2			7.6	15.4	
MERICAN HIGH-INCOME	♦♦	1210.7	52	4.75	0.89†	20.7	10.3	15.2	8.6	6.0	
ABSON BOND L	AVG	161.5	16	No load	0.97	15.9	7.6	9.1	6.8	12.5	
ERNSTEIN INTERMEDIATE DURATION	AVG	1260.8	50	No load	0.65	17.6	8.0	9.5	5.8	11.2	
ERNSTEIN SHORT DURATION PLUS	♦	535.2	6	No load	0.65	9.9	5.3	6.8	5.5	4.2	
ILTMORE FIXED-INCOME		175.2	21	4.50	0.71	17.9			5.8	6.4	
LANCHARD FLEXIBLE INCOME		229.9	–16	No load	1.58†	15.4	7.5		6.1	7.9	
OND FUND OF AMERICA	♦	6290.2	27	4.75	0.69†	18.2	8.6	11.6	7.5	11.3	
OLONIAL HIGH-YIELD SECURITIES A	♦♦♦	467.3	20	4.75	1.23†	17.6	12.0	19.6	9.1	8.0	
OLONIAL INCOME A	AVG	143.8	11	4.75	1.11†	20.3	8.9	10.8	7.2	13.4	
OLONIAL STRATEGIC INCOME A	♦♦	715.0	12	4.75	1.21†	20.2	10.2	13.5	8.1		
OLUMBIA FIXED-INCOME SECURITIES	AVG	316.3	25	No load	0.66	18.9	8.3	9.9	6.5	5.9	
EAN WITTER DIVERSIFIED INCOME		574.6	39	5.00**	1.51†	12.7	6.8		7.4		
EAN WITTER HIGH-INCOME SEC.		397.3	248	4.00**	1.55†	13.0			10.2	7.6	
EAN WITTER HIGH-YIELD SEC.	♦♦♦	447.1	3	5.50	0.79	17.1	12.7	24.3	11.5		
EAN WITTER INTERMEDIATE INCOME	AVG	231.9	3	5.00**	1.63†	13.7	6.2	8.2	6.0		
ELAWARE DELCHESTER A	♦♦	1021.8	8	4.75	1.09†	14.0	8.2	16.3	10.2	6.8	
G GOVERNMENT INCOME		184.7	4	2.00	0.68†	16.7	7.3		5.8	7.8	
ODGE & COX INCOME	AVG	303.3	55	No load	0.54	20.2	9.1	10.6	6.7	10.7	
REYFUS A BONDS PLUS	AVG	610.7	26	No load	0.99	20.3	9.1	10.8	6.3	11.7	
REYFUS SHORT-TERM INCOME		199.1	–11	No load	0.61	11.2	6.7		6.6	2.7	
REYFUS STRATEGIC INCOME	AVG	321.7	4	No load	0.94	20.8	9.2	11.1	6.3	10.9	
V MARATHON HIGH-INCOME	♦♦	488.8	18	5.00**	1.78†	13.9	9.3	16.3	9.5	7.2	
EDERATED BOND FORT. (a)	♦♦	216.6	52	1.00	1.03	20.2	10.5	17.8	7.6	13.5	
EDERATED HIGH-YIELD	♦♦♦	621.9	78	No load	0.85	18.4	10.7	18.9	9.2	6.6	
DELITY ADVISOR HIGH-YIELD A	♦♦♦	1267.6	86	3.50	1.15†	19.3	12.1	18.5	8.4	7.1	

ncludes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. NA = Not available. NM = Not meaningful
) Formerly Fortress Bond.
DATA: MORNINGSTAR, INC., CHICAGO, IL

MUTUAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
						TOTAL RETURN (%)					
		ASSETS $MIL.	% CHG. 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	1 YR.	3 YR.	5 YR.	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
FIDELITY ADVISOR INTERM. BOND A (b)		233.5	59	2.75	1.02†	12.2	6.9		6.0	4.8	
FIDELITY ADVISOR SHORT FIXED-INC. A	◆	540.8	–22	1.50	0.89†	9.8	5.1	7.2	5.9	2.3	
FIDELITY CAPITAL & INCOME	◆◆◆	2322.4	14	1.50*	0.96	16.7	11.6	18.3	9.6	6.2	
FIDELITY INTERMEDIATE BOND	◆	2821.4	33	No load	0.68	12.8	7.4	8.5	6.2	5.2	
FIDELITY INVESTMENT GRADE BOND	◆	1245.7	25	No load	0.75	15.5	8.3	10.4	6.3	7.6	
FIDELITY SHORT-TERM BOND	◆	1196.6	–21	No load	0.69	9.8	4.8	7.1	6.1	2.1	
FIDELITY SPARTAN HIGH-INCOME	◆◆◆	1080.6	75	1.00*	0.80	18.5	13.8	19.2	9.5	4.7	
FIDELITY SPARTAN INVMT. GRADE BOND		161.1	37	No load	0.65	18.6	9.2		6.3	7.9	
FIDELITY SPARTAN SHORT-TERM INCOME		479.6	–21	No load	0.65	9.9	4.6		6.3	2.2	
FIRST INVESTORS FUND FOR INC. A	◆◆◆	425.7	7	6.25	1.22†	19.5	12.1	18.6	9.4	5.7	
FIRST INVESTORS HIGH-YIELD A	◆◆	186.8	10	6.25	1.61†	19.4	11.6	17.3	10.0	6.6	
FIRST PRIORITY FIXED-INCOME INVMT.		156.3	NM	2.00	1.10†	16.0	6.0		5.2	8.0	
FPA NEW INCOME	◆◆	233.6	80	4.50	0.68	14.4	8.5	11.0	6.0	7.1	
FRANKLIN AGE HIGH INCOME I	◆◆◆	2075.9	21	4.25	0.66†	18.7	11.2	18.9	9.4	8.4	
HANCOCK HIGH-YIELD BOND B	◆◆	188.3	23	5.00**	1.89†	14.4	9.3	14.6	9.0	6.7	
HANCOCK SOVEREIGN BOND A	◆	1535.4	16	4.50	1.26†	19.5	8.9	10.2	7.2	14.3	
HANCOCK STRATEGIC INCOME A	◆◆	354.2	11	4.50	1.09†	18.7	9.4	13.5	9.0	9.0	
HARBOR BOND	◆	233.4	40	No load	0.70	19.2	8.8	11.0	6.9	11.6	
HOTCHKIS & WILEY LOW DURATION		157.5	123	No load	0.58	12.7			7.3	2.9	
IDS BOND A	◆	2560.7	20	5.00	0.78	22.0	10.5	12.5	6.9	15.8	
IDS EXTRA INCOME A	◆◆	1932.5	27	5.00	0.79	21.8	10.5	17.4	8.9	7.8	
IDS SELECTIVE A	AVG	1516.4	9	5.00	0.72	21.2	9.4	10.8	6.2	14.4	
INTERMEDIATE BOND FUND AMERICA	◆	1544.2	7	4.75	0.78†	13.9	6.4	7.9	6.6	4.8	
INVESCO HIGH-YIELD	◆◆	343.5	63	No load	1.00†	17.9	9.0	12.9	9.5	7.9	
INVESCO SELECT INCOME	◆◆	261.7	92	No load	1.00†	20.6	9.9	11.7	6.9	10.2	
JANUS FLEXIBLE INCOME	◆◆	620.5	75	No load	0.93	21.1	10.8	13.9	7.3	13.5	
KEMPER DIVERSIFIED INCOME A	◆◆◆	505.2	10	4.50	1.12	19.7	11.7	20.0	9.5	11.8	
KEMPER HIGH-YIELD A	◆◆◆	2565.2	14	4.50	0.90	17.5	11.6	19.0	10.3	7.5	
KEMPER INCOME & CAPITAL PRES. A	AVG	552.4	13	4.50	0.90	21.4	9.4	10.7	7.0	12.2	
KEYSTONE DIVERSIFIED BOND (B-2) (c)	◆	727.8	–1	4.00**	1.81†	14.7	6.7	9.6	7.5	11.3	
KEYSTONE HIGH-INCOME (B-4) (d)	AVG	675.7	1	4.00**	2.03†	9.8	6.8	15.3	10.6	7.0	
KEYSTONE QUALITY BOND (B-1) (e)	◆◆	309.2	–5	4.00**	1.86†	16.5	6.4	7.5	6.0	8.7	
KEYSTONE STRATEGIC INCOME B (f)		145.2	–5	5.00**	2.06†	10.2			8.2	6.8	
LIBERTY HIGH-INCOME BOND A	◆◆◆	519.0	23	4.50	1.21	19.2	11.2	20.9	9.2	6.5	
LIMITED TERM A		136.1	–20	1.00	1.10†	11.7	5.8		5.6	3.0	
LOOMIS SAYLES BOND		252.4	206	No load	0.84	32.0	15.7		6.7	19.3	
LORD ABBETT BOND-DEBENTURE	◆◆	1339.5	36	4.75	0.88†	17.5	9.4	16.0	9.4	8.8	
LORD ABBETT BOND-DEBENTURE TR.		147.6	134	1.00**	1.23†	15.9			7.7	9.5	
MAINSTAY HIGH-YIELD CORP. BOND B	◆◆◆	1601.2	43	5.00**	1.60†	19.7	13.9	18.9	10.2	5.5	
MARSHALL INTERMEDIATE BOND		357.6	10	No load	0.71	15.5	6.0		6.2	4.3	
MERRILL LYNCH CORP. HIGH-INCOME B	◆◆◆	3474.0	54	4.00**	1.32†	17.4	9.8	17.0	9.0	6.7	
MERRILL LYNCH CORP. INTERM.-TERM B		228.4	73	1.00**	1.11†	17.7	8.1		6.3	5.8	
MERRILL LYNCH CORP. INVMT. GRADE B	◆	688.7	46	4.00**	1.35†	18.9	7.7	9.2	6.0	10.6	
MERRILL LYNCH WORLD INCOME B		1241.9	–17	4.00**	1.54†	14.6	7.3		7.5	7.0	
MFS BOND A	AVG	534.6	23	4.75	1.00†	21.5	9.7	10.7	7.0	11.0	
MFS HIGH-INCOME A	◆◆◆	598.3	19	4.75	0.99†	17.2	10.9	18.9	8.5	7.8	
MFS INTERMEDIATE INCOME B	◆◆	230.0	–19	4.00**	2.22†	15.1	5.6	6.1	5.1		
NATIONWIDE BOND	◆◆	138.6	14	4.50	0.71	24.2	8.2	9.8	6.4	12.4	
NEUBERGER & BERMAN LIMITED MAT.	◆	303.8	3	No load	0.70	10.6	5.6	6.7	6.1	2.6	
NEW ENGLAND BOND INCOME A	AVG	200.2	29	4.50	1.08†	20.8	9.0	10.5	6.5	9.0	
NICHOLAS INCOME	◆◆	162.1	15	No load	0.59	16.2	9.4	12.2	8.6	6.4	
NORTHEAST INVESTORS	◆◆	805.2	45	No load	1.02	17.3	14.0	17.1	9.7	7.1	
NORTHSTAR ADV. HIGH-YIELD T (g)	◆◆◆	139.9	3	4.00**‡	1.34†	13.7	9.8	19.8	9.7	9.1	
OPPENHEIMER BOND A (h)	◆	168.5	75	4.75	1.06†	16.9	7.4	9.4	6.2		
OPPENHEIMER CHAMPION INCOME A (i)	◆◆	279.4	60	4.75	1.18†	14.7	11.6	16.2	8.5	7.5	
OPPENHEIMER HIGH-YIELD A	◆◆	1107.4	16	4.75	1.03†	15.1	10.6	14.7	9.5		
OPPENHEIMER STRATEGIC INCOME A	◆	3277.9	10	4.75	0.95†	15.4	9.6	11.3	9.0		
PAINEWEBBER HIGH-INCOME A	◆	235.0	–8	4.00	0.91†	11.0	6.3	17.0	11.4	7.3	
PAINEWEBBER INVMT. GRADE INCOME A	AVG	260.6	–2	4.00	0.97†	19.6	8.6	10.5	7.0	16.3	
PARAGON INTERMEDIATE-TERM BOND A	◆	314.4	7	4.50	0.76	17.3	6.9	8.5	6.2		
PARAGON SHORT-TERM GOVERNMENT A	AVG	128.3	–8	4.50	0.77	9.9	5.1	6.4	5.2		
PHOENIX HIGH-YIELD A	◆	505.7	0	4.75	1.19†	17.7	9.6	13.9	9.5	9.1	
PHOENIX MULTI-SECTOR FIXED-INC. A	◆	168.4	4	4.75	1.13†	19.8	8.9	13.2	7.4	9.9	
PIMCO ADV. HIGH-INCOME C	◆◆	167.8	13	1.00**	1.90†	20.0	6.1	7.5	7.5	5.6	
T. ROWE PRICE HIGH-YIELD	◆	1226.6	18	1.00*	0.88	15.8	9.1	14.3	9.1	8.3	
T. ROWE PRICE NEW INCOME	AVG	1668.1	22	No load	0.78	18.4	8.1	8.9	6.5	10.6	
T. ROWE PRICE SHORT-TERM BOND	AVG	464.4	–2	No load	0.79	9.7	4.3	5.8	6.3	2.8	
PRUDENTIAL HIGH-YIELD B	◆◆	2718.9	–18	5.00**	1.38†	17.2	10.0	15.5	9.3		
PUTNAM DIVERSIFIED INCOME B		1927.6	23	5.00**	1.76†	17.9			7.1	10.0	
PUTNAM HIGH YIELD A	◆◆	3060.8	13	4.75	0.95†	18.1	10.1	17.3	10.1	5.9	

* Includes redemption fee ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
(b) Formerly Fidelity Advisor Limited-Term Bond A. (c) Formerly Keystone Custodian B-2. (d) Formerly Keystone Custodian B-4. (e) Formerly Keystone Custodian B-1. (f) Formerly Keystone America Strategic Income B. (g) Formerly Advantage High-Yield Bond. (h) Formerly Oppenheimer Investment Grade Bond A. (i) Formerly Oppenheimer Champion High-Yield A.

DATA: MORNINGSTAR, INC., CHICAGO, IL

IUTUAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
						TOTAL RETURN (%)					
		ASSETS $MIL.	% CHG. 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	1 YR.	3 YR.	5 YR.	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
UTNAM HIGH YIELD ADVANTAGE A	♦♦♦	890.1	34	4.75	1.03†	18.8	10.9	18.7	10.3		
UTNAM INCOME A	♦	967.2	27	4.75	1.05†	19.8	9.1	11.0	6.6	11.1	
CUDDER INCOME	AVG	579.4	25	No load	0.97	18.5	8.4	9.8	6.3	11.2	
CUDDER SHORT-TERM BOND	AVG	1818.2	–15	No load	0.73	10.7	5.1	6.9	6.2	3.0	
ELIGMAN HIGH-YIELD BOND A	♦♦♦	182.1	209	4.75	1.13†	20.7	13.2	17.9	9.4	7.2	
EVEN SEAS YIELD PLUS		1380.6	14	No load	0.38†	6.6	4.7		5.8	0.5	
784 INCOME		211.8	24	No load	0.55†	18.0			6.1	9.9	
IERRA CORPORATE INCOME A	♦	357.1	–1	4.50	0.90†	27.1	9.9	11.9	7.1	20.7	
MITH BARNEY DIVR STRAT. INCOME B	AVG	2401.8	7	4.50**	1.56†	15.1	7.8	9.6	7.9	6.7	
MITH BARNEY HIGH-INCOME B	♦♦	521.0	30	4.50**	1.61†	17.5	9.9	16.5	9.3		
MITH BARNEY INVMT. GRADE BOND B	♦♦	289.1	34	4.50**	1.57†	34.9	13.0	13.9	6.2	29.1	
TATE ST RESEARCH HIGH-INCOME A (j)	♦♦	623.7	5	4.50	1.23†	12.4	10.5	17.3	10.1	5.8	
TEINROE INCOME	♦	207.1	35	No load	0.82	19.7	9.3	10.8	6.9	6.9	
TEINROE INTERMEDIATE BOND	AVG	312.8	11	No load	0.70	16.8	7.5	9.0	6.4	6.1	
TRONG ADVANTAGE	♦♦	989.7	9	No load	0.80	7.5	6.4	7.6	6.6	1.0	
TRONG CORPORATE BOND (k)	♦	259.3	110	No load	1.10	25.4	13.1	12.7	7.0	10.5	
TRONG SHORT-TERM BOND	♦	1105.0	6	No load	0.90	12.0	6.3	8.0	6.9	2.6	
WENTIETH CENTURY LONG-TERM BOND	AVG	152.5	27	No load	0.78	20.3	8.2	9.4	6.1	10.2	
NITED BOND A	♦	563.5	9	5.75	0.72†	20.5	8.7	10.4	6.3	15.0	
NITED HIGH-INCOME A	♦♦	980.9	8	5.75	0.84†	17.8	10.1	16.4	8.8	8.3	
NITED HIGH-INCOME II A	♦♦	368.7	7	5.75	0.88†	16.9	9.6	14.9	8.6	7.6	
AN KAMPEN AMER. CAP. CORP. BOND A (l)	AVG	174.7	8	4.75	1.09†	21.2	9.0	10.4	6.7		
AN KAMPEN AMER. CAP. HI-INC. CORP. A (m)	♦♦	416.7	15	4.75	1.10†	17.4	10.5	17.5	9.5	7.8	
AN KAMPEN AMER. CAP. HIGH-YIELD A (n)	♦♦	268.5	12	4.75	1.32†	17.5	10.1	16.1	8.1	6.9	
ANGUARD BOND IDX. INTRM.-TERM BOND		345.6	384	No load	0.18	21.0			6.3	7.6	
ANGUARD BOND IDX. SHORT-TERM BOND		207.6	170	No load	0.18	12.9			6.2	2.7	
ANGUARD BOND IDX. TOTAL BOND	AVG	2405.0	39	No load	0.18	18.2	8.1	9.3	6.4	8.8	
ANGUARD FIXED-INC. HIGH-YLD. CORP.	♦♦	2900.0	37	1.00*	0.34	19.2	11.5	15.3	8.6	7.9	
ANGUARD FIXED-INC. I/T CORP. BOND		361.4	139	No load	0.28	21.4			6.5	7.3	
ANGUARD FIXED-INC. L/T CORP. BOND	AVG	3356.1	31	No load	0.32	26.4	11.1	12.7	6.6	20.0	
ANGUARD FIXED-INC. S/T CORPORATE	♦	3743.3	29	No load	0.28	12.7	6.4	7.9	6.1	2.4	
ICTORY INTERMEDIATE INCOME		171.3	48	4.75	0.79	14.1			6.0	4.2	
ICTORY INVESTMENT QUALITY BOND		127.7	36	4.75	0.79	16.7			6.0		
ICTORY LIMITED-TERM INCOME	AVG	171.3	124	2.00	0.79	11.1	5.2	6.4	5.6		
ILLIAM BLAIR INCOME SHARES	♦	147.3	2	No load	0.68	14.4	7.0	8.8	6.2	4.7	
OVERNMENT											
ARP GNMA & U.S. TREASURY	AVG	5257.3	0	No load	0.67	12.8	5.5	7.5	6.6	6.9	
IM INTERMEDIATE GOVERNMENT A (o)	♦	175.5	11	4.75	1.04†	16.3	6.3	7.6	7.3	8.1	
IM LTD. MATURITY TREASURY RET.	♦	312.5	17	1.00	0.51†	9.4	4.8	6.1	5.8	1.5	
LLIANCE BOND U.S. GOVERNMENT B		754.4	7	3.00**	1.72†	15.5	6.2		6.8	7.2	
LLIANCE MORTGAGE SEC. INCOME B		738.7	–20	3.00**	2.00†	14.5	5.3		6.0		
SSET MANAGEMENT ADJ. RATE MORTGAGE		898.2	4	No load	0.47†	9.1	5.2		6.1	0.7	
SSET MANAGEMENT INTERM MORT. SEC.	♦	178.9	–15	No load	0.39†	13.9	6.2	8.5	6.3	3.7	
SSET MANAGEMENT SHORT U.S. GOVT.	♦	168.9	2	No load	0.47†	11.4	5.7	7.1	6.2	2.2	
TLAS U.S. GOVT. & MORTGAGE SEC. A	AVG	255.6	4	3.00	0.80†	15.5	6.3	8.4	6.7		
ENHAM ADJUSTABLE RATE GOVT. SEC.		313.4	–29	No load	0.57	8.8	3.7		5.8	0.6	
ENHAM GNMA INCOME	♦	1111.4	17	No load	0.58	15.8	6.7	8.6	6.9	6.3	
ENHAM TARGET MATURITIES 2000	♦♦	299.7	18	No load	0.59	20.7	8.6	10.7	0.0	5.0	
ENHAM TARGET MATURITIES 2005	♦♦♦	228.5	125	No load	0.64	32.6	11.8	13.1	0.0	9.9	
ENHAM TARGET MATURITIES 2010	♦♦♦	120.7	117	No load	0.68	42.1	15.6	15.2	0.0	14.7	
ENHAM TARGET MATURITIES 2015	♦♦♦	140.7	15	No load	0.68	52.7	16.2	15.6	0.0	19.8	
ENHAM TARGET MATURITIES 2020	♦♦♦	726.1	498	No load	0.70	61.3	20.4	16.3	0.0	24.6	
ENHAM TREASURY NOTE	AVG	307.4	4	No load	0.53	13.7	6.2	7.7	5.6	3.7	
ERNSTEIN GOVT. SHORT DURATION	♦	146.6	2	No load	0.69	9.9	4.9	6.3	5.3	2.5	
ARDINAL GOVERNMENT OBLIGATIONS	♦	150.0	–5	4.50	0.76	14.0	5.7	7.2	7.7	13.4	
OLONIAL FEDERAL SECURITIES A	♦	1240.4	0	4.75	1.18†	20.4	8.3	9.2	6.5	6.7	
OLONIAL U.S. GOVERNMENT A	AVG	1129.8	72	4.75	1.11†	14.9	6.1	6.8	6.2	15.0	
OMMON SENSE GOVERNMENT	♦	331.7	2	6.75	0.89	16.9	6.3	8.2	6.5	7.2	
OMPOSITE U.S. GOVERNMENT SEC. A	♦	177.3	–6	4.00	0.97†	19.4	7.1	8.4	5.8	9.9	
EAN WITTER FEDERAL SECURITIES	♦	844.9	4	5.00**	1.52†	18.8	7.2	8.4	6.0	12.5	
EAN WITTER SHORT-TERM U.S. TREAS.		290.7	–12	No load	0.84†	9.8	4.4		5.2	2.0	
EAN WITTER U.S. GOVT. SECURITIES	AVG	7938.7	–3	5.00**	1.22†	16.7	6.5	7.3	6.2	7.4	
ELAWARE LIMITED-TERM GOVT. A (p)	AVG	651.7	–17	3.00	0.91†	8.7	4.0	6.0	7.7	3.3	
ELAWARE U.S. GOVERNMENT A	♦	194.7	–6	4.75	1.23†	13.7	4.9	7.2	8.0	5.8	
REYFUS 100% U.S. TREASURY INTERM.	AVG	196.2	5	No load	0.89	15.8	7.3	8.8	6.8	6.5	
REYFUS 100% U.S. TREASURY L/T	♦♦	145.5	17	No load	0.98	24.9	9.8	11.0	6.2	13.9	
REYFUS 100% U.S. TREASURY S/T	♦	187.8	9	No load	0.35	11.4	5.9	7.5	6.8	2.6	
REYFUS GNMA	AVG	1445.1	1	No load	0.97†	15.1	6.2	7.9	6.6	9.9	
REYFUS SHORT-INTERM. GOVERNMENT	♦	574.3	22	No load	0.47	12.6	6.3	7.8	6.5	2.6	

Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful. Formerly MetLife-State St. Research High-Inc. A. (k) Formerly Strong Income. (l) Formerly American Capital Corporate Bond A. (m) Formerly American Capital High-Yield Investments. A (n) ormerly Van Kampen Merritt High-Yield A. (o) Formerly AIM Government Securities A. (p) Formerly Delaware Treasury Resrv. Interm. A.

DATA: MORNINGSTAR, INC., CHICAGO, IL

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
						TOTAL RETURN (%)					
		ASSETS $MIL.	% CHG 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	1 YR.	3 YR	5 YR.	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
EV TRADITIONAL GOVT. OBLIGATIONS	AVG	359.9	–7	3.75	1.73†	14.0	6.9	8.0	7.4	4.6	
EVERGREEN U.S. GOVERNMENT B (q)		187.2	–4	5.00**	1.79†	15.9			6.0	8.1	
FIDELITY ADVISOR GOVT. INVMT. A		221.2	79	3.50	0.89†	17.7	7.5	8.4	5.9	8.7	
FIDELITY GINNIE MAE	AVG	805.6	14	No load	0.75	16.6	6.7	8.1	6.6	6.1	
FIDELITY GOVERNMENT SECURITIES		994.1	63	No load	0.71	18.1	7.9	9.5	6.0	9.0	
FIDELITY MORTGAGE SECURITIES		486.5	39	No load	0.77	17.0	8.4	8.7	6.8	5.3	
FIDELITY SHORT-INTERMEDIATE GOVT.		133.2	–12	No load	0.82	11.9	5.2		6.4	2.6	
FIDELITY SPARTAN GINNIE MAE	AVG	445.0	28	No load	0.65	16.7	6.9	8.1	6.6	5.6	
FIDELITY SPARTAN GOVT. INCOME	AVG	249.0	7	No load	0.65	18.2	6.9	8.5	6.2	9.3	
FIDELITY SPARTAN LTD. MAT. GOVT.		829.5	0	No load	0.65	13.9	6.3	7.3	6.2	5.4	
FIDELITY SPARTAN LONG-TERM GOVT.		116.6	63	No load	0.65	30.4	10.1	11.1	5.7	23.7	
FIRST INVESTORS GOVERNMENT A		216.3	–1	6.25	1.42†	15.6	5.0	7.1	6.9	7.6	
FORTIS U.S. GOVERNMENT SEC. E		457.3	–7	4.50‡	0.77	15.2	5.6	7.2	6.3	5.4	
FORTRESS ADJUST RATE U.S. GOVT.		321.5	–26	1.00**	1.02†	8.3	3.8		5.7	4.5	
FRANKLIN ADJUSTABLE U.S. GOVT. SEC.		491.9	–28	2.25	0.40†	9.2	2.8	4.2	5.9	0.8	
FRANKLIN SHORT-INTRM. U.S. GOVT. I		211.6	–4	2.25	0.65†	11.1	5.4	7.0	5.3	2.2	
FRANKLIN TAX-ADVANT. U.S. GOVT.		403.6	–12	4.25	0.61†	18.3	7.1	8.6	6.5	7.8	
FRANKLIN U.S. GOVERNMENT SEC. I	AVG	11105.9	1	4.25	0.61†	16.7	6.7	8.2	7.0	7.0	
FUND FOR U.S. GOVERNMENT SEC. A	AVG	1375.9	1	4.50	0.95†	14.4	5.6	7.0	7.1	6.5	
GALAXY II U.S. TREASURY INDEX RET.		128.1	22	No load	0.40	18.1	7.8		6.1	8.3	
GOVERNMENT INCOME SECURITIES	AVG	2355.8	–8	2.00**	0.97	14.8	5.6	7.2	7.0	6.0	
GRADISON-McDONALD GOVT. INCOME		185.4	1	2.00	0.90†	17.2	6.7	8.0	6.3	5.3	
HANCOCK GOVERNMENT INCOME A		468.7	NM	4.50	0.12†	18.4			7.4	20.0	
HANCOCK LIMITED-TERM GOVT. A	AVG	198.7	–8	3.00	1.41†	11.3	5.6	6.7	5.7	6.1	
HANCOCK SOVEREIGN U.S. GOVT. A		375.4	21	4.50	1.23†	18.5	7.5		6.4	21.3	
IDS FEDERAL INCOME A	AVG	1083.3	7	5.00	0.79	14.0	6.4	7.3	6.4	12.9	
INVESTORS TRUST GOVERNMENT B		1073.1	–11	5.00**	1.76†	13.5	3.6	6.0	6.9	7.8	
ISI TOTAL RETURN U.S. TREASURY		209.5	7	4.45	0.77†	21.7	9.9	10.1	6.1	12.4	
KEMPER ADJ. RATE U.S. GOVT. A	AVG	125.7	–21	3.50	0.93	8.5	4.3	6.4	5.8	4.8	
KEMPER SHORT-INTERMEDIATE GOVT. B		200.0	–12	4.00**	1.87†	10.4	4.3	5.8	5.8	2.9	
KEMPER U.S. GOVERNMENT SEC. A		4652.8	–2	4.50	0.75	18.4	6.8	8.4	7.2	11.2	
KEMPER U.S. MORTGAGE A		2086.1	13	4.50	0.89	18.1	6.4		7.2	11.1	
KIEWIT SHORT-TERM GOVERNMENT		156.4	15	No load	0.37	9.0			5.6	2.0	
LEGG MASON U.S. GOVT. INT.-TM. PRIM.	AVG	231.3	–2	No load	0.90†	14.1	6.1	7.7	5.4	6.0	
LEXINGTON GNMA INCOME	AVG	130.7	–1	No load	0.98	15.9	7.0	8.4	7.1		
LORD ABBETT U.S. GOVT.		3313.3	3	4.75	0.90†	16.2	6.5	8.8	8.9	7.6	
LORD ABBETT U.S. GOVT. SEC. TR.		327.7	1	1.00**	1.64†	15.4			8.0	6.9	
MAINSTAY GOVERNMENT B		990.6	–3	5.00**	1.70†	15.7	6.0	7.0	6.4	8.7	
MARQUIS GOVERNMENT SECURITIES A		143.7	29	3.50	0.70	14.1			5.4	4.6	
MARSHALL GOVERNMENT INCOME		114.7	46	No load	0.86	17.0	6.4		6.3	9.1	
MERRILL LYNCH FEDERAL SECURITIES B		1216.1	–6	4.00**	1.33†	14.5	5.5		6.1	5.1	
MFS GOVERNMENT LTD. MATURITY A	AVG	248.2	–3	2.50	0.89†	10.4	5.4	6.2	6.6	4.0	
MFS GOVERNMENT MORTGAGE B		703.5	–34	4.00**	1.96†	15.6			5.1		
MFS GOVERNMENT SECURITIES A		338.7	8	4.75	0.79†	19.5	8.2	9.2	6.1	11.3	
NEW ENGLAND ADJ. RATE U.S. GOVT. A		329.7	–33	1.00	0.60†	8.6	4.4		6.0	0.9	
NEW ENGLAND GOVERNMENT SEC. A		147.6	0	4.50	1.29†	20.0	7.3	8.7	6.2	10.0	
NEW ENGLAND LTD.-TERM U.S. GOVT. A		362.1	–12	3.00	1.18†	12.9	5.5	7.2	7.0	5.0	
NORTHERN U.S. GOVERNMENT		143.6	30	No load	0.90	12.6			5.0		
NORTHSTAR ADV. GOVERNMENT SEC. T (r)		150.6	–1	4.00**‡	1.29†	22.9	9.5	10.6	6.0		
OPPENHEIMER LIMITED-TERM GOVT. A	AVG	373.7	51	3.50	0.99†	10.4	6.2	7.6	7.5		
OPPENHEIMER U.S. GOVERNMENT A	AVG	522.8	75	4.75	1.09†	14.9	7.0	8.2	7.0		
OVERLAND EXP. VARIABLE RATE GOVT. A		653.9	–46	3.00	0.79†	7.7	2.8	4.2	5.7	1.7	
PAINEWEBBER LOW DUR. U.S. GOVT. INC. C (s)		173.4	–34	No load	1.36†	10.1			5.2	1.1	
PAINEWEBBER U.S. GOVT. INCOME A		428.2	3	4.00	0.95†	17.0	3.7	6.4	6.3	14.5	
PERMANENT PORTFOLIO TREASURY BILL		115.5	–5	No load	0.82	4.9	3.5	3.7	2.7	0.2	
PHOENIX U.S. GOVERNMENT SECURITIES A		239.8	–6	4.75	0.98†	17.2	6.9	8.5	5.5	6.7	
PIMCO ADVISORS U.S. GOVERNMENT C		286.8	–8	1.00**	1.80†	17.3	6.0	7.2	5.3	10.8	
PIONEER AMERICA INCOME A		162.0	0	4.50	1.00†	16.1	6.7	7.8	6.6	7.5	
PREMIER GNMA A	AVG	134.4	–5	4.50	0.94	15.4	6.6	8.3	6.2	11.4	
T. ROWE PRICE GNMA		896.5	19	No load	0.76	17.8	7.1	8.5	6.9	8.1	
T. ROWE PRICE U.S. INTERMEDIATE	AVG	183.4	12	No load	0.69	15.9	6.9	8.3	6.0	5.0	
PRINCOR GOVERNMENT SEC. INCOME A		267.5	8	4.75	0.87†	19.2	7.4	8.9	6.2	9.6	
PRUDENTIAL GOVERNMENT INCOME A		938.0	2019	4.00	0.98†	19.7	7.4	8.8	6.4	8.0	
PRUDENTIAL GOVT. SHORT-INTERM. TERM (t)	AVG	210.9	–6	No load	0.84†	12.9	5.7	7.2	5.5	3.3	
PRUDENTIAL MORTGAGE INCOME B (u)		125.5	–49	5.00**	1.73†	14.8	5.2	6.7	5.9	6.0	
PUTNAM AMERICAN GOVERNMENT INCOME A		2183.0	–3	4.75	0.83†	18.4	6.8	7.1	6.8	12.8	
PUTNAM FEDERAL INCOME A		428.4	0	4.75	1.06†	19.0	6.5	8.1	5.7	10.8	
PUTNAM U.S. GOVERNMENT INCOME A	AVG	2903.1	–3	4.75	0.85†	16.2	6.2	7.4	6.9	10.5	
SCHWAB SHORT/INTERMED. GOVT. BOND		156.3	–2	No load	0.58	10.9	5.1		6.1	2.7	
SCUDDER GNMA	AVG	436.8	5	No load	0.95	16.6	6.2	8.1	6.3	9.6	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful. (q) Formerly First Union U.S. Government C Invmt. (r) Formerly Advantage Government Securities. (s) Formerly PaineWebber Short-Term US Govt. Inc. D. (t) Formerly Prudential Government Interm. Term. (u) Formerly Prudential GNMA B.

DATA: MORNINGSTAR, INC., CHICAGO, IL

	RATING	SIZE ASSETS $MIL.	SIZE % CHG. 1994-95	FEES SALES CHARGE (%)	FEES EXPENSE RATIO (%)	PERFORMANCE TOTAL RETURN (%) 1 YR.	PERFORMANCE TOTAL RETURN (%) 3 YR.	PERFORMANCE TOTAL RETURN (%) 5 YR.	PORTFOLIO YIELD (%)	PORTFOLIO MATURITY (YEARS)	TREND 5-YEAR ANALYSIS
784 U.S. GOVT. MEDIUM-TERM INCOME		157.8	44	No load	0.80†	15.9			6.1	5.9	
IERRA U.S. GOVERNMENT A		438.1	–5	4.50	0.95†	16.5	5.4	7.4	7.0		
MITH BARNEY ADJUST. RATE GOVT. A		171.2	–9	No load	2.47†	7.8	4.4		5.9		
MITH BARNEY GOVERNMENT SEC. A		448.1	–7	4.50	1.00†	14.8	7.3		7.1	7.4	
MITH BARNEY MANAGED GOVT. A		515.5	–6	4.50	1.07†	13.8	6.8	8.5	6.0		
MITH BARNEY U.S. GOVT. SEC. A	AVG	383.4	6	4.50	0.56†	16.5	6.9	8.6	6.8		
MITH BREEDEN SH. DUR. U.S. GOVT. SER.		235.6	21	No load	0.11	6.1	4.9		6.8	0.5	
TAGECOACH GINNIE MAE A		166.2	–3	4.50	0.73†	17.5	6.8		6.8		
TAGECOACH U.S. GOVT. ALLOCATION A		135.6	–3	4.50	1.01†	14.9	7.9	9.4	5.2	6.4	
TATE ST. RESEARCH GOVT. INCOME A	AVG	655.8	8	4.50	1.07†	17.6	7.9	9.2	6.3	8.9	
TRONG GOVERNMENT SECURITIES		504.9	82	No load	0.90	19.9	9.3	10.7	6.1	6.9	
UNAMERICA U.S. GOVT. SEC. B		499.6	–21	4.00**	2.15†	14.9	5.6	6.4	5.4	8.5	
HORNBURG LTD.-TERM U.S. GOVT. A	AVG	142.8	–20	2.50	0.95†	13.0	5.5	7.3	6.0	3.6	
WENTIETH CENTURY U.S. GOVT. SH.-TERM	AVG	391.5	2	No load	0.70	10.5	4.7	6.0	5.4	2.4	
S. GOVERNMENT SECURITIES		1361.9	6	4.75	0.79†	15.5	6.7	8.4	7.4	7.6	
NITED GOVERNMENT SECURITIES A		155.2	2	4.25	0.82†	19.3	8.1	9.6	6.1		
SAA GNMA		297.7	22	No load	0.32	16.8	7.7		6.9	8.2	
ALUE LINE U.S. GOVERNMENT		248.5	–14	No load	0.66	14.4	3.9	6.8	6.5	5.2	
AN KAMPEN AMER. CAP. GOVT. SEC. A (v)		2554.5	–1	4.75	1.02†	16.8	6.5	8.4	6.5		
AN KAMPEN AMER. CAP. U.S. GOVT. A (w)		2955.0	1	4.75	1.00†	17.6	6.4	8.2	7.3	8.0	
AN KAMPEN AMER. CAP. U.S. GOVT. INC. B (x)		191.2	–8	4.00**	1.82†	14.6	4.9		6.7		
ANGUARD FIXED-INC. GNMA		6907.7	20	No load	0.30	17.0	7.1	8.9	7.0	6.7	
ANGUARD FIXED-INC. I/T U.S. TREAS.		1195.3	42	No load	0.28	20.4	8.7		6.1	7.5	
ANGUARD FIXED-INC. L/T U.S. TREAS.		917.4	42	No load	0.28	30.1	12.2	12.2	6.1	21.2	
ANGUARD FIXED-INC. S/T FEDERAL		1403.7	–7	No load	0.28	12.3	6.0	7.2	5.8	2.3	
ANGUARD FIXED-INC. S/T U.S. TREAS.		869.4	23	No load	0.28	12.1	5.9		6.0	2.4	
CTORY GOVERNMENT MORTGAGE		134.7	–13	4.75	0.76	15.2	6.9	8.3	6.4	14.3	
RTUS U.S. GOVT. SEC. INVMT. (y)	AVG	120.9	17	2.00**	0.99†	13.8	5.8	7.6	6.3	6.3	
PG GOVERNMENT SECURITIES		171.4	–21	No load	0.80	13.3	4.1	6.7	6.2	5.2	
RIGHT U.S. TREASURY NEAR TERM (z)	AVG	143.0	–33	No load	0.70†	11.9	5.4	7.1	6.0	2.8	
UNICIPAL											
ARP INSURED T/F GENERAL BOND		1839.2	5	No load	0.69	16.1	7.1	8.4	4.8	15.2	
M MUNICIPAL BOND A	AVG	284.4	10	4.75	0.89†	13.0	6.7	8.5	5.6	15.9	
LIANCE MUNI INCOME CA A	AVG	490.9	12	4.25	0.64†	23.9	7.9	8.8	5.4	25.5	
LIANCE MUNI INCOME NATIONAL A		346.4	9	4.25	0.62†	22.3	7.8	9.1	5.4	25.0	
LIANCE MUNI INCOME NY A		186.7	9	4.25	0.66†	21.2	7.1	8.8	5.5	26.0	
LIANCE MUNI INSURED CA A		107.7	16	4.25	0.82†	24.1	7.7	8.6	5.0	25.3	
LIANCE MUNI INSURED NATIONAL A		167.6	12	4.25	0.66†	22.5	7.9	9.0	5.1	23.4	
MERICAN HIGH-INCOME MUNI BOND		195.9	105	4.75	0.62†	19.0			5.8	11.7	
LAS CA MUNICIPAL BOND A		184.3	7	3.00	0.57†	14.8	7.1	8.3	4.8	18.9	
NHAM CA MUNICIPAL HIGH-YIELD		130.7	36	No load	0.51	18.3	8.2	8.9	5.9	22.7	
NHAM CA TAX-FREE INSURED		190.7	18	No load	0.50	19.0	8.1	8.9	5.1	18.5	
NHAM CA TAX-FREE INTERM.-TERM		426.9	8	No load	0.48	13.5	6.5	7.4	4.8	7.5	
NHAM CA TAX-FREE LONG-TERM	AVG	295.9	19	No load	0.49	19.8	8.4	9.0	5.4	20.3	
NHAM CA TAX-FREE SHORT-TERM		100.9	–5	No load	0.51	8.3	4.5		4.1	2.8	
RNSTEIN CA MUNICIPAL		224.2	39	No load	0.70	13.6	6.0	6.8	4.4	7.8	
RNSTEIN DIVERSIFIED MUNICIPAL		709.3	41	No load	0.67	12.8	6.1	7.0	4.6	6.9	
RNSTEIN NY MUNICIPAL		487.1	29	No load	0.67	12.8	6.1	7.1	4.6	7.3	
RNSTEIN SHORT DUR. DIVERS. MUNI		102.5	16	No load	0.72	6.2			4.2	1.9	
LIFORNIA INVMT. TAX-FREE INCOME		207.9	12	No load	0.62	20.6	8.1	9.1	4.7	16.5	
LVERT TAX-FREE RES. LTD.-TERM A		457.9	–16	2.00	0.66	5.6	4.0	4.7	4.2	0.9	
URCHILL TAX-FREE OF KY		230.2	–1	4.00	0.72†	13.7	7.1	7.9	5.6	14.1	
LONIAL CA TAX-EXEMPT A		307.1	4	4.75	0.77†	19.5	7.0	8.0	5.2	24.2	
LONIAL HIGH-YIELD MUNICIPAL B		139.2	21	5.00**	1.90†	16.0	6.8		5.8	24.5	
LONIAL MA TAX-EXEMPT A	AVG	209.7	12	4.75	0.72†	18.4	7.7	9.1	5.3	21.6	
LONIAL TAX-EXEMPT A		3122.7	10	4.75	1.01†	17.6	6.9	8.1	5.5	22.7	
LONIAL TAX-EXEMPT INSURED A		241.8	18	4.75	1.05†	17.4	6.9	8.0	4.9	22.2	
LUMBIA MUNICIPAL BOND		383.8	13	No load	0.57	14.1	6.4	7.5	5.1	13.7	
MMON SENSE MUNICIPAL BOND		122.1	13	4.75	0.99	16.6	7.3	8.3	5.2	19.8	
MPOSITE TAX-EXEMPT BOND A		230.1	7	4.00	0.79†	18.3	7.6	8.6	4.8	12.9	
VIS TAX-FREE HIGH INCOME B (aa)		123.9	–13	4.00**	2.14†	7.8	6.1	7.7	5.2	16.3	
AN WITTER CA TAX-FREE INCOME	AVG	1048.2	4	5.00**	1.32†	15.0	6.3	7.3	4.7	20.6	
AN WITTER MULTI-STATE MUNI CA		119.4	7	4.00	0.58	19.2	7.5		5.2	21.4	
AN WITTER NY TAX-FREE INCOME		215.2	4	5.00**	1.40†	16.6	6.3	8.1	4.5	18.0	
AN WITTER TAX-EXEMPT SEC.	AVG	1314.1	2	4.00‡	0.47	17.4	7.2	8.7	5.5	20.4	
LAWARE TAX-FREE PA A		1012.9	7	4.75	0.90†	14.7	6.9	8.5	5.6	21.7	
LAWARE TAX-FREE USA A		772.3	8	4.75	0.92†	13.7	7.2	8.7	5.9	22.3	
EYFUS CA INTERMEDIATE MUNI		235.4	–1	No load	0.32	13.4	7.0		4.7	8.9	
EYFUS CA TAX-EXEMPT BOND		1521.2	6	No load	0.71	14.1	5.8	6.9	5.4	19.8	

cludes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful. Formerly American Capital Government SEC. A. (w) Formerly Van Kampen Merritt U.S. Government A. (x) Formerly American Capital U.S. Govt. Income B. (y) Formerly Medalist U.S. Govern- nt SEC. Invmt. (z) Formerly Wright Near Term Bond. (aa) Formerly Venture Muni (+) Plus B.

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
		ASSETS $Mil.	% CHG. 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%) 1 YR.	3 YR	5 YR	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
DREYFUS CT INTERMEDIATE MUNI		134.1	8	No load	0.34	14.3	7.1		4.5	7.9	
DREYFUS FL INTERMEDIATE MUNI		425.4	4	No load	0.48	14.0	6.9		4.6	8.1	
DREYFUS INSURED MUNICIPAL BOND	♦♦♦	241.7	12	No load	0.94†	15.6	5.9	7.4	5.1	24.6	
DREYFUS INTERMEDIATE MUNI BOND	♦♦	1550.3	7	No load	0.73	14.2	6.7	8.0	5.1	9.4	
DREYFUS MA TAX-EXEMPT BOND	♦	158.3	8	No load	0.80	15.5	6.9	8.1	5.4	21.3	
DREYFUS MUNICIPAL BOND	AVG	3938.0	9	No load	0.70	15.7	6.7	8.1	5.5	21.8	
DREYFUS NJ INTERMEDIATE MUNI		230.3	8	No load	0.45	14.1	6.8		4.5	7.6	
DREYFUS NJ MUNICIPAL BOND	♦	651.5	13	No load	0.77	15.3	7.0	8.3	5.5	19.2	
DREYFUS NY INSURED TAX-EXEMPT BOND	♦	157.3	4	No load	0.98†	15.4	6.2	8.0	5.0	24.6	
DREYFUS NY TAX-EXEMPT BOND	AVG	1879.8	11	No load	0.72	16.2	6.8	8.3	5.2	19.2	
DREYFUS NY TAX-EXEMPT INTERM. BOND	♦	371.6	10	No load	0.96†	14.0	6.5	8.0	4.6	8.9	
DREYFUS SHORT-INTERM. MUNI BOND	♦♦♦	336.4	–21	No load	0.70†	7.1	4.4	5.6	4.5	1.9	
DUPREE KY TAX-FREE INCOME	♦♦	293.8	19	No load	0.63	14.2	7.7	8.6	5.3	17.6	
EMPIRE BUILDER TAX-FREE BOND	♦	116.6	12	No load	0.95	14.6	7.1	8.2	4.8	7.5	
EV MARATHON AL MUNICIPALS (bb)		111.4	12	5.00**	1.43†	17.2	6.6		4.4	22.4	
EV MARATHON AZ MUNICIPALS (cc)		143.0	4	5.00**	1.53†	19.6	7.5		4.5	21.1	
EV MARATHON CA MUNICIPALS	♦♦♦	405.9	2	5.00**	1.65†	18.5	6.3	6.9	4.9	22.5	
EV MARATHON CT MUNICIPALS (dd)		194.3	10	5.00**	1.55†	17.9	5.9		4.7	21.7	
EV MARATHON FL LTD. MAT. MUNIS (ee)		126.3	–17	3.00**	1.50†	10.7	5.3		3.7	6.8	
EV MARATHON FL MUNICIPALS (ff)	♦♦♦	713.2	0	5.00**	1.54†	18.4	6.7	8.3	4.7	24.2	
EV MARATHON GA MUNICIPALS (gg)		121.4	1	5.00**	1.41†	16.4	5.7		4.5	21.8	
EV MARATHON KY MUNICIPALS (hh)		144.3	8	5.00**	1.44†	18.0	6.4		4.5	21.9	
EV MARATHON MA MUNICIPALS (ii)		297.2	8	5.00**	1.58†	17.3	6.1		4.8	23.7	
EV MARATHON MD MUNICIPALS (jj)		117.5	7	5.00**	1.43†	18.9	6.6		4.5	23.5	
EV MARATHON MI MUNICIPALS (kk)		189.1	5	5.00**	1.51†	18.0	6.5		4.5	21.3	
EV MARATHON NATL. LTD. MAT. MUNIS (ll)		121.6	–16	3.00**	1.57†	9.8	5.0		4.0	5.6	
EV MARATHON NATL. MUNICIPALS	♦	2279.9	11	5.00**	1.53†	19.8	8.1	9.2	5.6	24.8	
EV MARATHON NC MUNICIPALS (mm)		192.4	8	5.00**	1.42†	16.7	5.7		4.5	20.3	
EV MARATHON NJ MUNICIPALS (nn)		407.2	4	5.00**	1.53†	15.9	6.2		4.8	25.0	
EV MARATHON NY LTD. MAT. MUNIS (oo)		145.1	–13	3.00**	1.51†	11.0	5.1		3.8	5.7	
EV MARATHON NY MUNICIPALS (pp)	♦♦♦	654.4	8	5.00**	1.55†	17.9	6.7	8.7	4.8	20.9	
EV MARATHON OH MUNICIPALS (qq)		318.9	6	5.00**	1.59†	17.9	6.6		4.6	19.0	
EV MARATHON OR MUNICIPALS (rr)		146.6	7	5.00**	1.43†	18.0	6.6		4.3	21.0	
EV MARATHON PA MUNICIPALS (ss)		489.0	2	5.00**	1.51†	17.2	6.0		4.7	21.6	
EV MARATHON VA MUNICIPALS (tt)		194.5	9	5.00**	1.44†	18.0	6.3		4.5	22.1	
EVERGREEN FL MUNICIPAL BOND A (uu)		128.9	NM	4.75	0.82†	19.6			5.1	18.9	
EXCELSIOR INTRM.-TERM TAX-EXEMPT (vv)	♦	250.3	10	4.50	0.61	15.0	6.9	7.9	4.4	8.2	
FIDELITY ADVISOR HIGH-INC. MUNI A	AVG	572.0	13	3.50	0.91†	16.7	6.9	8.8	5.7	18.4	
FIDELITY AGGRESSIVE TAX-FREE	♦♦	907.7	14	1.00*	0.63	14.9	7.2	8.5	6.1	17.5	
FIDELITY CA TAX-FREE HIGH-YIELD	AVG	507.7	14	No load	0.56	19.2	7.2	8.1	5.3	16.2	
FIDELITY CA TAX-FREE INSURED	♦♦♦	226.1	15	No load	0.59	19.5	6.9	8.2	5.0	17.3	
FIDELITY HIGH-YIELD TAX-FREE	AVG	1794.4	7	No load	0.56	16.2	6.8	7.8	5.4	14.6	
FIDELITY INSURED TAX-FREE	♦♦	356.3	12	No load	0.58	18.7	7.7	8.5	5.0	14.1	
FIDELITY LIMITED-TERM MUNICIPALS	♦	941.1	7	No load	0.56	14.8	7.1	8.1	5.1	7.9	
FIDELITY MA TAX-FREE HIGH-YIELD	♦	1179.3	19	No load	0.54	18.1	7.6	8.7	5.6	17.1	
FIDELITY MI TAX-FREE HIGH-YIELD	AVG	491.2	13	No load	0.57	15.4	6.7	8.3	5.3	16.0	
FIDELITY MN TAX-FREE	AVG	314.2	13	No load	0.59	16.0	6.8	7.3	5.5	16.0	
FIDELITY MUNICIPAL BOND	♦♦	1078.9	7	No load	0.53	18.2	6.8	8.3	4.9	12.6	
FIDELITY NY TAX-FREE HIGH-YIELD	AVG	434.2	14	No load	0.58	19.6	7.5	9.0	5.1	15.2	
FIDELITY NY TAX-FREE INSURED	♦	335.8	12	No load	0.58	18.5	7.2	8.5	4.8	13.5	
FIDELITY OH TAX-FREE HIGH-YIELD	♦	403.1	15	No load	0.57	16.4	7.4	8.4	5.3	14.2	
FIDELITY SPARTAN CA MUNI HIGH-YIELD	AVG	406.6	9	0.50*	0.55	19.0	7.3	8.4	5.4	17.3	
FIDELITY SPARTAN CT MUNI INCOME (ww)	♦	357.6	14	0.50*	0.55	17.1	7.2	8.1	5.4	16.7	
FIDELITY SPARTAN FL MUNI INCOME		403.0	19	0.50*	0.54	18.6	8.4		5.1	15.5	
FIDELITY SPARTAN INTERM. MUNI		223.0	8	No load	0.42	14.4			4.7	8.2	
FIDELITY SPARTAN MUNI INCOME	AVG	579.9	8	0.50*	0.55	18.6	7.6	8.8	5.4	14.6	
FIDELITY SPARTAN NJ MUNI HIGH-YIELD	♦	366.4	12	0.50*	0.55	15.4	7.2	8.5	5.4	16.1	
FIDELITY SPARTAN NY MUNI HIGH-YIELD	AVG	325.9	14	0.50*	0.55	19.1	7.4	9.2	5.2	15.1	
FIDELITY SPARTAN PA MUNI HIGH-YIELD	♦♦	287.5	19	0.50*	0.55	17.4	8.1	9.2	5.5	15.0	
FIDELITY SPARTAN SH.-INTERM. MUNI	♦♦♦	904.9	–1	No load	0.55	8.5	5.2	6.1	4.2	3.3	
FIRST INVESTORS INSURED TAX-EXEMPT A	♦	1368.6	5	6.25	1.18†	16.6	6.4	7.5	5.5	19.0	
FIRST INVESTORS NY INSURED T/F A	AVG	213.9	11	6.25	1.31†	16.0	6.4	7.8	5.4	21.0	
FLAGSHIP ALL-AMERICAN TAX-EXEMPT A	♦	205.7	22	4.20	0.76†	17.5	8.1	9.9	5.6	21.8	
FLAGSHIP CT DOUBLE TAX-EXEMPT A	♦	209.1	11	4.20	0.73†	16.6	7.1	8.3	5.5	19.3	
FLAGSHIP FL DOUBLE TAX-EXEMPT A	♦	343.1	5	4.20	0.73†	16.4	7.6	8.9	5.3	20.0	
FLAGSHIP GA DOUBLE TAX-EXEMPT A	♦♦	114.6	7	4.20	0.83†	17.0	7.0	8.1	5.4	20.4	
FLAGSHIP KS TRIPLE TAX-EXEMPT A		103.0	37	4.20	0.54†	17.7	7.2		5.3	19.8	
FLAGSHIP KY TRIPLE TAX-EXEMPT A	AVG	415.1	17	4.20	0.68†	17.3	7.6	8.9	5.5	20.2	
FLAGSHIP LIMITED-TERM TAX-EXEMPT A	♦♦♦	508.4	–12	2.50	0.74†	10.3	5.7	7.1	4.7	4.8	
FLAGSHIP MI TRIPLE TAX-EXEMPT A	AVG	257.1	13	4.20	0.80†	16.3	7.3	8.6	5.4	18.3	

*Includes redemption fee. **Includes deferred sales charge. †12(b)-1 plan in effect. ‡Not currently accepting new accounts or deposits. NA=Not available. NM=Not meaningful. (bb) Formerly EV Marathon AL T/F. (cc) Formerly EV Marathon AZ T/F. (dd) Formerly EV Marathon CT T/F. (ee) Formerly EV Marathon FL Ltd. Mat. T/F. (ff) Formerly EV Marathon FL T/F. (gg) Formerly EV Marathon GA T/F. (hh) Formerly EV Marathon KY T/F. (ii) Formerly EV Marathon MA T/F. (jj) Formerly EV Marathon MD T/F. (kk) Formerly EV Marathon MI T/F. (ll) Formerly EV Marathon Natl. Ltd. Mat. T/F. (mm) Formerly EV Marathon NC T/F. (nn) Formerly EV Marathon NJ T/F. (oo) Formerly EV Marathon NY Ltd. Mat. T/F. (pp) Formerly EV Marathon NY T/F. (qq) Formerly EV Marathon OH T/F. (rr) Formerly EV Marathon OR T/F. (ss) Formerly EV Marathon PA T/F. (tt) Formerly EV Marathon VA T/F. (uu) Formerly First Union FL Muni Bond B Invmt. (vv) Formerly UST Master Interm-Term T/E. (ww) Formerly Fidelity Spartan CT Muni High-Yield.

DATA: MORNINGSTAR, INC., CHICAGO

UTUAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
						TOTAL RETURN (%)					
		ASSETS $MIL.	% CHG. 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	1 YR.	3 YR.	5 YR.	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
.AGSHIP MO DOUBLE TAX-EXEMPT A	AVG	221.2	21	4.20	0.67†	16.3	7.4	8.7	5.4	19.4	
.AGSHIP NC DOUBLE TAX-EXEMPT A (xx)	AVG	194.4	9	4.20	0.91†	15.4	6.6	8.1	5.3	18.3	
.AGSHIP OH DOUBLE TAX-EXEMPT A	▲	461.1	11	4.20	0.95†	15.5	7.1	8.3	5.4	17.7	
.AGSHIP TN DOUBLE TAX-EXEMPT A	AVG	252.4	15	4.20	0.89†	15.7	6.9	8.3	5.3	18.6	
.AGSHIP VA DOUBLE TAX-EXEMPT A	AVG	119.7	17	4.20	0.79†	16.3	7.3	8.7	5.4	20.0	
)RTRESS MUNICIPAL INCOME	AVG	429.1	4	2.00*	1.08†	15.9	6.6	7.8	5.8	23.9	
:ANKLIN AL TAX-FREE INCOME I	▲▲	185.2	15	4.25	0.72†	15.3	7.3	8.6	5.5	20.3	
:ANKLIN AZ TAX-FREE INCOME I	▲▲	750.7	8	4.25	0.60†	14.6	6.9	8.6	5.6	17.4	
:ANKLIN CA INSURED TAX-FREE INC. I	▲	1572.6	15	4.25	0.59†	16.3	7.6	8.4	5.4	18.9	
:ANKLIN CA TAX-FREE INCOME I	▲▲	13555.9	9	4.25	0.55†	15.0	7.0	8.2	6.0	19.3	
:ANKLIN CO TAX-FREE INCOME I	▲▲	214.2	17	4.25	0.70†	16.1	7.4	8.8	5.5	20.7	
:ANKLIN CT TAX-FREE INCOME I	▼	167.1	13	4.25	0.71†	14.3	6.7	7.8	5.6	20.2	
:ANKLIN FEDERAL TAX-FREE INC. I	▲▲	7210.6	10	4.25	0.59†	15.1	7.2	8.9	6.2	18.8	
:ANKLIN FL TAX-FREE INCOME I	▲▲	1366.3	10	4.25	0.59†	14.7	7.5	8.7	5.8	17.9	
:ANKLIN GA TAX-FREE INCOME I	▲▲	127.7	15	4.25	0.76†	14.1	7.1	8.4	5.5	19.3	
:ANKLIN HIGH YIELD TAX-FREE INC. I	▲▲▲	3694.1	18	4.25	0.60†	16.3	8.7	9.5	6.5	19.7	
:ANKLIN INSURED TAX-FREE INC. I	▲▲	1722.7	6	4.25	0.59†	13.6	7.0	8.3	5.7	17.1	
:ANKLIN LA TAX-FREE INCOME I	▲	107.8	7	4.25	0.75†	14.6	6.6	8.2	5.7	18.9	
:ANKLIN MA INSURED TAX-FREE INC. I	▲▲	298.9	9	4.25	0.67†	14.1	7.1	8.3	5.6	16.2	
:ANKLIN MD TAX-FREE INCOME I	▲	172.8	19	4.25	0.73†	17.3	7.7	8.8	5.4	18.8	
:ANKLIN MI INSURED TAX-FREE INC. I	▲▲	1111.5	12	4.25	0.61†	13.9	7.0	8.3	5.6	15.9	
:ANKLIN MN INSURED TAX-FREE INC. I	▲▲	490.1	8	4.25	0.66†	13.3	6.7	7.8	5.5	15.8	
:ANKLIN MO TAX-FREE INCOME I	▲	245.5	14	4.25	0.70†	15.7	7.6	8.7	5.3	18.4	
:ANKLIN NC TAX-FREE INCOME I	▲	243.4	19	4.25	0.70†	16.1	6.9	8.2	5.5	18.5	
:ANKLIN NJ TAX-FREE INCOME I	▲	568.7	12	4.25	0.63†	15.6	6.7	8.3	5.4	19.5	
:ANKLIN NY INSURED TAX-FREE INC. I		256.2	14	4.25	0.56†	18.5	7.5		5.2	22.8	
:ANKLIN NY TAX-FREE INCOME I	▲▲	4861.4	10	4.25	0.57†	13.6	7.0	9.1	6.2	21.1	
:ANKLIN OH INS. TAX-FREE INCOME I	▲	684.1	9	4.25	0.63†	14.4	7.1	8.2	5.5	17.2	
:ANKLIN OR TAX-FREE INCOME I	▲	372.9	12	4.25	0.65†	15.1	6.7	8.2	5.3	18.3	
:ANKLIN PA TAX-FREE INCOME I	▲▲▲	637.5	13	4.25	0.63†	14.4	7.3	9.0	5.9	18.0	
:ANKLIN PR TAX-FREE INCOME I	▲	191.2	13	4.25	0.73†	14.5	6.8	8.3	5.7	19.4	
:ANKLIN TX TAX-FREE INCOME I	▲▲	131.4	3	4.25	0.73†	13.3	7.1	8.4	5.7	17.2	
:ANKLIN VA TAX-FREE INCOME I	▲▲	271.1	11	4.25	0.69†	15.5	7.4	8.7	5.5	18.8	
:NERAL CA MUNICIPAL BOND	AVG	333.5	12	No load	0.76†	18.0	7.6	8.5	5.2	21.5	
:NERAL MUNICIPAL BOND	AVG	966.5	17	No load	0.87	17.3	7.2	9.2	5.4	21.0	
:NERAL NY MUNICIPAL BOND	AVG	335.3	14	No load	0.76	16.7	7.3	9.2	5.2	21.5	
:NCOCK CA TAX-FREE INCOME A	▼	309.3	28	4.50	0.69†	21.9	7.9	9.0	5.4	23.8	
:NCOCK HIGH-YIELD TAX-FREE B	▲▲	159.8	7	5.00**	1.85†	18.9	7.7	8.7	5.4	24.0	
:NCOCK MANAGED TAX-EXEMPT B	▼	178.1	–14	5.00**	1.62†	15.7	6.8	8.3	4.6	22.7	
:NCOCK TAX-EXEMPT INCOME A	▼	495.8	6	4.50	1.11†	16.6	7.1	8.3	5.2	22.8	
:NCOCK TAX-FREE BOND A	▼▼	118.8	4	4.50	0.85†	20.2	7.9	9.8	5.3	25.7	
:WAIIAN TAX-FREE	▲	676.0	10	4.00	0.75†	15.4	6.6	7.6	5.3	15.3	
:ARTLAND WI TAX-FREE		118.5	16	No load	0.85	17.8	6.9		5.0	19.3	
5 CA TAX-EXEMPT A	AVG	247.6	7	5.00	0.65	15.1	6.9	8.0	5.3	22.3	
5 HIGH-YIELD TAX-EXEMPT A	▲	6363.4	14	5.00	0.59	17.4	6.9	8.3	5.9	21.0	
5 INSURED TAX-EXEMPT A	▼▼	527.9	8	5.00	0.66	16.9	7.6	8.7	5.1	23.0	
5 MN TAX-EXEMPT A	AVG	415.7	11	5.00	0.67	15.0	7.0	8.1	5.5	21.2	
5 NY TAX-EXEMPT A	▼	124.0	9	5.00	0.70	13.4	6.3	8.2	5.5	22.6	
5 TAX-EXEMPT BOND A	▼▼▼	1172.6	8	5.00	0.61	18.8	7.6	7.9	5.0	20.3	
VESCO TAX-FREE LONG-TERM BOND	AVG	261.2	3	No load	0.92†	15.6	7.0	8.4	4.9	21.0	
:NSAS MUNICIPAL	▲▲	135.8	13	4.25	0.82†	15.7	6.8	7.9	5.1	19.6	
MPER MUNICIPAL BOND A	▼▼	3554.0	4	4.50	0.60	18.3	8.2	9.2	5.1	19.0	
MPER STATE TAX-FREE INC. CA A	AVG	1103.2	4	4.50	0.74	19.5	8.4	9.0	5.1	20.0	
MPER STATE TAX-FREE INC. FL A		122.4	2	4.50	0.80	18.4	8.9		4.9	18.8	
MPER STATE TAX-FREE INC. NY A	▲	321.2	5	4.50	0.81	18.0	8.2	9.5	5.0	19.0	
YSTONE TAX-EXEMPT	▼	686.8	1	4.00**	1.65†	16.6	6.1	7.3	5.1	18.0	
YSTONE TAX-FREE	▼	1204.5	1	4.00**‡	1.55†	16.6	6.3	7.4	5.0	19.9	
EWIT TAX-EXEMPT		141.9	–30	No load	0.39	10.1			4.1	5.7	
BENTHAL NY MUNICIPAL BOND		107.9	41	4.50	0.64	21.4	8.0		5.3	11.1	
GG MASON MD TAX-FREE INCOME		149.6	12	2.75	0.54†	14.8	7.5		4.9	15.4	
ERTY MUNICIPAL SECURITIES A	AVG	714.5	6	4.50	0.92	13.0	6.2	7.9	6.0	24.4	
MITED TERM NY MUNICIPAL A		567.7	15	2.00	0.89†	10.6	6.6		5.5	10.9	
MITED TERM TAX-EXMPT BOND AMER.		209.5	15	4.75	0.64†	12.4			4.7	5.3	
RD ABBETT CA TAX-FREE INC.	▼▼▼	301.7	4	4.75	0.76†	17.8	6.3	8.2	5.7	18.3	
RD ABBETT TAX-FREE INCOME CT		115.9	15	4.75	0.41†	17.7	7.4		5.9	18.3	
RD ABBETT TAX-FREE INCOME FL		176.7	3	4.75	0.32†	17.2	6.8		5.7	21.4	
RD ABBETT TAX-FREE INCOME MO		136.6	17	4.75	0.74†	17.6	7.0		5.7	18.2	
RD ABBETT TAX-FREE INCOME NATL.	▼▼	668.0	9	4.75	0.82†	18.1	7.1	8.5	5.8	21.0	
RD ABBETT TAX-FREE INCOME NJ	AVG	195.0	11	4.75	0.72†	17.7	7.9	9.3	5.7	23.7	
RD ABBETT TAX-FREE INCOME NY	▼▼▼	335.1	6	4.75	0.82†	16.3	6.0	8.1	5.8	14.7	

ıcludes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful
Formerly Flagship NC Triple Tax-Exempt A

DATA: MORNINGSTAR, INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

Bond Fund

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
		ASSETS $MIL.	% CHG. 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%) 1 YR.	3 YR.	5 YR.	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
LORD ABBETT TAX-FREE INCOME TX	◆◆	102.9	8	4.75	0.62†	18.4	7.7	9.0	5.7	18.4	
MAINSTAY TAX-FREE BOND B	◆	543.3	6	5.00**	1.20†	14.9	6.0	7.5	5.1	22.0	
MERRILL LYNCH CA MUNI BOND B	◆◆	573.3	–8	4.00**	1.16†	17.1	6.7	7.7	4.9	20.7	
MERRILL LYNCH FL MUNI BOND B		218.7	9	4.00**	1.21†	15.9	6.0		4.7	23.0	
MERRILL LYNCH MUNI INSURED B	◆◆◆	787.7	5	4.00**	1.19†	16.6	6.5	7.8	4.8	20.0	
MERRILL LYNCH MUNI INTERM.-TERM B	AVG	184.2	44	1.00**	1.04†	11.8	5.9	7.2	4.8	10.8	
MERRILL LYNCH MUNI NATIONAL B	◆◆	419.9	5	4.00**	1.32†	17.1	6.6	7.9	5.0	23.2	
MERRILL LYNCH NJ MUNI BOND B	◆	164.4	4	4.00**	1.25†	14.7	6.1	7.4	4.7	21.1	
MERRILL LYNCH NY MUNI BOND B	◆◆	536.9	–8	4.00**	1.18†	15.7	5.4	7.7	4.8	20.7	
MERRILL LYNCH PA MUNI BOND B	AVG	128.8	10	4.00**	1.28†	16.6	7.4	8.6	4.9	19.9	
MFS AR MUNICIPAL BOND A		184.2	4	4.75	0.75†	15.0	6.7		5.1	18.4	
MFS CA MUNICIPAL BOND A	◆	272.3	5	4.75	0.69†	18.0	7.0	8.5	5.4	16.0	
MFS MA MUNICIPAL BOND A	AVG	261.7	5	4.75	1.17†	16.0	6.8	8.2	5.5	17.6	
MFS MD MUNICIPAL BOND A	◆◆	144.7	2	4.75	1.21†	15.1	6.1	7.2	5.1	17.9	
MFS MUNICIPAL BOND A	◆◆	2002.6	6	4.75	0.61	17.4	7.7	9.0	5.2	17.2	
MFS MUNICIPAL HIGH-INCOME A	◆◆◆	1003.9	12	4.75‡	1.04	16.2	7.4	8.1	7.0	23.8	
MFS MUNICIPAL INCOME B	AVG	335.8	–20	4.00**	2.16†	13.8	6.1	7.5	4.8	18.5	
MFS NC MUNICIPAL BOND A	◆◆	425.3	3	4.75	1.16†	16.3	6.4	7.5	4.9	18.9	
MFS NY MUNICIPAL BOND A	AVG	142.3	–1	4.75	1.07†	16.8	7.5	9.2	5.0	19.0	
MFS SC MUNICIPAL BOND A	◆	174.7	9	4.75	1.19†	15.9	6.9	7.9	5.0	18.3	
MFS TN MUNICIPAL BOND A	AVG	114.5	2	4.75	1.22†	14.8	6.9	7.8	5.2	18.3	
MFS VA MUNICIPAL BOND A	◆◆	440.6	8	4.75	1.16†	16.7	6.5	7.6	5.2	17.2	
MFS WV MUNICIPAL BOND A	AVG	134.2	11	4.75	1.19†	15.0	6.8	7.8	5.2	18.0	
NATIONWIDE TAX-FREE INCOME	◆◆	267.2	13	5.00**	0.99†	17.5	6.4	7.9	5.0	19.6	
NEW ENGLAND MA TAX-FREE INCOME A	◆	120.2	12	4.25	0.85†	17.8	7.0	8.3	5.3	10.5	
NEW ENGLAND MUNICIPAL INCOME A (yy)	◆◆◆	195.4	6	4.50	0.92†	17.2	6.7	8.1	5.4	10.0	
NEW YORK MUNI	◆◆◆	226.9	6	No load	3.21†	15.6	1.2	6.0	3.6	19.6	
NORTHERN INTERMEDIATE TAX-EXEMPT		238.4	10	No load	0.85	11.9			3.9	6.3	
NORTHERN TAX-EXEMPT		125.4	5	No load	0.85	17.4			4.4	14.4	
NUVEEN MUNICIPAL BOND R	◆◆◆	2917.5	13	No load‡	0.59	15.3	7.1	8.1	5.5	19.8	
OPPENHEIMER CA TAX-EXEMPT A	◆	285.4	30	4.75	0.96†	19.8	7.4	8.4	5.5	23.0	
OPPENHEIMER NY TAX-EXEMPT A	◆◆	712.4	14	4.75	0.90†	17.7	6.7	8.3	5.5	20.7	
OPPENHEIMER TAX-FREE BOND A	◆◆◆	635.1	17	4.75	0.88†	18.3	6.8	8.4	5.5	21.0	
OVERLAND EXP. CA TAX-FREE BOND A	◆◆	268.4	–2	4.50	0.50†	16.4	8.0	8.9	5.4	17.6	
PACIFIC HORIZON CA TAX-EXEMPT BD.	◆	220.6	17	4.50	0.95	16.5	7.3	8.3	5.0	19.2	
PAINEWEBBER CA TAX-FREE INCOME A	◆◆◆	157.8	–8	4.00	0.88†	16.8	6.3	7.5	5.1	21.0	
PAINEWEBBER NATIONAL T/F INC. A	◆◆◆	331.9	–1	4.00	0.88†	16.0	6.6	7.7	5.0	19.0	
PARAGON LA TAX-FREE A	◆	205.1	5	4.50	0.65	11.9	6.1	7.3	4.9	9.5	
PHOENIX CA TAX-EXEMPT BONDS A	AVG	122.3	8	4.75	0.93†	19.2	7.3	8.0	5.7	13.2	
PHOENIX TAX-EXEMPT BOND A	◆◆	148.6	6	4.75	0.96†	18.3	7.5	8.9	5.3	12.4	
PIONEER TAX-FREE INCOME A	◆	475.2	5	4.50	0.91†	16.9	7.3	8.6	5.2	19.3	
PIPER MN TAX-EXEMPT	AVG	138.1	0	4.00	0.89†	19.4	8.1	8.7	5.3	19.9	
PREMIER CA MUNICIPAL BOND A	◆	185.6	–1	4.50	0.90	17.4	7.8	8.5	5.0	20.2	
PREMIER MUNICIPAL BOND A	AVG	502.2	3	4.50	0.92	17.4	7.9	9.5	5.7	22.7	
PREMIER NY MUNICIPAL BOND A	AVG	145.8	5	4.50	0.89	18.5	8.0	9.7	4.9	20.4	
PREMIER STATE MUNI BOND CT A	◆	336.8	4	4.50	0.89	15.5	7.1	8.2	5.4	19.5	
PREMIER STATE MUNI BOND FL A	AVG	246.0	–2	4.50	0.90	16.7	7.6	8.9	5.2	21.3	
PREMIER STATE MUNI BOND MD A	AVG	300.1	2	4.50	0.90	15.9	7.1	8.3	5.1	21.1	
PREMIER STATE MUNI BOND MI A	◆	178.1	5	4.50	0.92	17.5	8.4	9.5	5.1	20.1	
PREMIER STATE MUNI BOND MN A	AVG	143.4	1	4.50	0.90	15.3	7.4	8.4	5.3	21.0	
PREMIER STATE MUNI BOND OH A	◆◆	271.7	2	4.50	0.92	15.5	7.5	8.8	5.4	20.5	
PREMIER STATE MUNI BOND PA A	AVG	219.1	4	4.50	0.92	17.7	7.9	9.1	5.2	21.1	
T. ROWE PRICE CA TAX-FREE BOND	◆	146.8	20	No load	0.60	17.4	7.6	8.7	5.2	18.3	
T. ROWE PRICE MD TAX-FREE BOND	◆	799.9	18	No load	0.57	16.5	7.6	8.5	5.4	16.8	
T. ROWE PRICE NY TAX-FREE BOND	◆◆	134.9	22	No load	0.60	17.3	7.7	9.2	5.3	18.7	
T. ROWE PRICE TAX-FREE HIGH-YIELD	◆◆◆	982.8	23	No load	0.79	16.6	8.0	9.0	5.9	20.4	
T. ROWE PRICE TAX-FREE INCOME	AVG	1397.3	11	No load	0.59	17.7	7.9	9.0	5.3	18.3	
T. ROWE PRICE TAX-FREE SHORT-INTRM.	◆◆◆	450.8	0	No load	0.59	8.1	4.9	5.7	4.3	3.7	
T. ROWE PRICE VA TAX-FREE BOND		177.8	24	No load	0.65	16.8	7.7		5.1	18.8	
PRINCOR TAX-EXEMPT BOND A	◆◆	183.2	14	4.75	0.83†	20.7	7.1	8.6	5.3	21.9	
PRUDENTIAL CA MUNI CA B	AVG	102.1	–37	5.00**	1.13†	17.5	7.2	8.1	5.2	16.8	
PRUDENTIAL MUNI BOND HIGH-YIELD B	◆◆	898.7	–8	5.00**	1.09†	16.3	7.6	8.6	5.6	19.9	
PRUDENTIAL MUNI BOND INSURED B	◆◆	516.8	–16	5.00**	1.14†	16.3	6.9	8.1	4.3	18.0	
PRUDENTIAL MUNICIPAL FL A	◆	118.0	–3	3.00	0.20†	19.1	7.8	9.1	5.6	21.4	
PRUDENTIAL MUNICIPAL NJ B	AVG	236.0	–16	5.00**	0.98†	16.1	6.8	8.2	4.9	18.2	
PRUDENTIAL MUNICIPAL NY A	◆	174.2	NM	3.00	0.69†	17.8	7.6	9.2	5.3	17.8	
PRUDENTIAL MUNICIPAL PA B	AVG	200.7	–15	5.00**	1.15†	16.5	6.9	8.4	5.1	17.9	
PRUDENTIAL NATIONAL MUNICIPALS A	◆	541.3	NM	3.00	0.77†	17.1	7.4	8.7	5.2	18.7	
PUTNAM AZ TAX EXEMPT INCOME A		137.6	6	4.75	0.70†	17.1	7.0		5.1	21.9	
PUTNAM CA TAX EXEMPT INCOME A	AVG	3286.7	9	4.75	0.74†	19.1	7.9	8.7	5.4	22.0	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
(yy) Formerly New England Tax-Exempt Income A.

DATA: MORNINGSTAR, INC., CHICAGO, I

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
						TOTAL RETURN (%)					
		ASSETS $MIL.	% CHG. 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	1 YR.	3 YR.	5 YR.	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
UTNAM FL TAX EXEMPT INCOME A	▼	270.5	3	4.75	0.83†	17.3	7.0	8.5	5.1	22.6	
UTNAM MA TAX EXEMPT INCOME A (zz)	▲▲	265.6	17	4.75	0.89†	18.2	7.6	9.4	5.7	22.5	
UTNAM MI TAX EXEMPT INCOME A (aaa)	AVG	143.2	17	4.75	0.95†	16.4	7.1	8.5	5.5	21.4	
UTNAM MUNICIPAL INCOME A	▲	850.5	8	4.75	0.95†	18.7	7.6	9.3	5.6	21.0	
UTNAM NJ TAX EXEMPT INCOME A	▼	243.6	9	4.75	0.95†	16.3	7.0	8.2	5.4	23.6	
UTNAM NY TAX EXEMPT INCOME A	▼▼▼	2016.6	5	4.75	0.75†	15.5	6.6	8.9	5.4	20.9	
UTNAM NY TAX EXEMPT OPPORT A	▲▲▲	180.5	9	4.75	1.01†	16.4	7.3	8.3	5.5	23.2	
UTNAM OH TAX EXEMPT INCOME A (bbb)	▲	196.5	8	4.75	0.93†	15.7	7.0	8.3	5.4	20.4	
UTNAM PA TAX EXEMPT INCOME A	▲	187.2	16	4.75	0.92†	16.8	7.7	9.1	5.4	20.8	
UTNAM TAX EXEMPT INCOME A	▼▼▼	2347.4	11	4.75	0.78†	17.6	7.1	8.8	5.5	23.0	
UTNAM TAX FREE HIGH YIELD B	▲▲	1486.1	8	5.00**	1.51†	16.0	7.1	8.7	5.5	21.9	
UTNAM TAX-FREE INSURED B	▼▼	389.2	1	5.00**	1.54†	17.0	6.8	7.7	4.5	22.0	
OCHESTER FUND MUNICIPALS	▲	2144.7	20	4.00	0.84†	19.3	7.8	9.5	6.0	22.4	
AFECO MUNICIPAL BOND	▼▼	520.3	20	No load	0.56	21.5	7.9	9.2	5.3	22.0	
CUDDER CA TAX-FREE	AVG	307.3	12	No load	0.80	18.9	7.9	9.1	4.7	13.6	
CUDDER HIGH-YIELD TAX-FREE	AVG	302.8	17	No load	0.80	18.8	7.4	9.3	5.5	11.3	
CUDDER LIMITED-TERM TAX-FREE		119.2	24	No load	0.00	9.4			4.6	3.8	
CUDDER MA TAX-FREE	▲	323.0	16	No load	0.47	17.9	8.1	9.5	5.1	11.0	
CUDDER MANAGED MUNICIPAL BONDS	▼	773.5	9	No load	0.63	16.8	7.5	8.7	5.1	11.0	
CUDDER MEDIUM-TERM TAX-FREE	▲▲	710.0	1	No load	0.63	14.3	7.0	8.4	4.8	7.2	
CUDDER NY TAX-FREE	▼	197.0	8	No load	0.82	17.9	7.3	9.3	4.8	13.1	
ELIGMAN TAX-EXEMPT MA A	▲	118.1	5	4.75	0.85†	15.2	7.1	8.6	5.1	18.8	
ELIGMAN TAX-EXEMPT MI A	AVG	155.2	8	4.75	0.84†	15.8	7.1	8.5	5.1	19.2	
ELIGMAN TAX-EXEMPT MN A	AVG	132.9	2	4.75	0.85†	11.4	7.2	7.1	5.7	14.6	
ELIGMAN TAX-EXEMPT NATIONAL A	▼▼▼	107.9	0	4.75	0.85†	20.1	7.3	8.2	5.0	26.2	
ELIGMAN TAX-EXEMPT OH A	AVG	173.7	6	4.75	0.84†	15.2	6.9	8.1	5.3	17.3	
ELIGMAN TAX-EXEMPT SC A	▼▼	116.2	9	4.75	0.83†	17.7	7.0	8.2	5.0	17.5	
ENTINEL TAX-FREE INCOME	▼	111.7	13	5.00	0.75†	15.2	7.2	8.5	4.9	18.6	
'84 TAX-EXEMPT MED.-TERM INCOME		192.3	112	No load	0.80†	14.3			4.8	7.7	
ERRA CA MUNICIPAL A	▼▼	401.4	1	4.50	0.85†	18.1	7.0	8.0	5.5	21.0	
ERRA NATIONAL MUNICIPAL A	▼	257.3	–6	4.50	0.83†	15.6	7.3	9.4	5.5	20.0	
T TAX-FREE INCOME	▲▲▲	281.9	16	No load	0.79	12.9	7.4	7.8	5.5	15.1	
ITH BARNEY CA MUNICIPALS A	▼	589.9	63	4.00	0.80†	22.0	8.7	9.1	5.4	19.9	
ITH BARNEY MANAGED MUNIS A	▲	1872.2	–9	4.00	0.71†	20.3	10.0	10.7	5.8	22.4	
ITH BARNEY MUNI FL A		123.0	19	4.00	0.61†	17.4	8.0		5.5	21.8	
ITH BARNEY MUNI LTD. TERM A	▲▲▲	229.9	–6	2.00	0.61†	11.4	6.3	7.2	5.4	6.9	
ITH BARNEY MUNI NATIONAL A	▲	397.1	3	4.00	0.60†	18.9	8.3	9.4	5.7	22.4	
ITH BARNEY NJ MUNICIPALS A	▼	163.2	54	4.00	0.89†	17.1	7.1	8.6	5.4	21.7	
ITH BARNEY NY MUNICIPALS A	AVG	490.8	6	4.00	0.63†	17.2	6.6	8.4	5.8	23.0	
ITH BARNEY TAX-EXEMPT INCOME B	AVG	728.2	0	4.50**	1.35†	15.7	6.5	7.9	5.3	22.0	
TAGECOACH CA TAX-FREE BOND A		296.4	–3	4.50	0.65†	18.2	7.7		5.0	15.9	
TATE ST. RESEARCH TAX-EXEMPT A (ccc)	▼▼	252.8	6	4.50	1.20†	16.6	6.8	8.3	4.9	19.0	
TEINROE HIGH-YIELD MUNICIPALS	AVG	282.8	6	No load	0.86	17.7	7.6	7.6	5.5	19.3	
TEINROE INTERMEDIATE MUNICIPALS	▲	217.8	1	No load	0.74	12.9	6.6	7.6	4.6	8.6	
TEINROE MANAGED MUNICIPALS	AVG	637.4	5	No load	0.65	16.6	7.0	8.6	5.2	17.3	
TRONG HIGH-YIELD MUNI BOND		267.0	148	No load	0.00	14.6			7.0	18.7	
TRONG MUNICIPAL BOND	▲	246.7	–12	No load	0.80	11.4	5.9	8.6	5.2	20.0	
TRONG SHORT-TERM MUNICIPAL BOND		132.7	–18	No load	0.70	5.4	3.5		4.8	2.6	
JNAMERICA TAX-EXEMPT INSURED A	▼	130.7	–6	4.75	1.20†	15.7	6.2	6.8	4.6	16.2	
AX-EXEMPT BOND FUND OF AMERICA	▲	1501.6	20	4.75	0.66†	17.3	7.6	8.6	5.5	11.3	
AX-EXEMPT FUND OF CA	▲	250.9	21	4.75	0.73†	17.6	8.0	8.5	5.3	12.0	
AX-FREE FUND OF CO	▲	219.2	10	4.00	0.57†	13.3	6.6	7.9	5.1	10.1	
AX-FREE TRUST OF AZ	▲	395.2	10	4.00	0.74†	15.3	6.6	8.2	5.2	15.0	
AX-FREE TRUST OF OR	▲	313.3	5	4.00	0.71†	13.9	6.5	7.6	5.1	15.3	
IORNBURG INTERMEDIATE MUNI A		222.1	6	3.50	1.00†	13.2	7.4		5.1	8.1	
IORNBURG LTD.-TERM MUNI NATL. A	▲▲▲	917.4	–10	2.50	0.97†	10.0	5.6	6.6	4.7	3.9	
IORNBURG NM INTERMEDIATE MUNI A		135.2	–7	3.50	0.90†	11.2	6.4		4.6	6.9	
ITED MUNICIPAL BOND A	▼▼	1022.0	14	4.25	0.65†	20.2	8.5	9.7	5.1	18.3	
ITED MUNICIPAL HIGH-INCOME A	▲▲▲	392.4	16	4.25	0.76†	16.7	8.6	9.6	6.4	21.4	
AA CA BOND	▼▼	414.8	24	No load	0.44	21.9	7.6	8.4	5.6	24.8	
AA TAX-EXEMPT INTERM.-TERM	▲▲	1673.1	18	No load	0.40	15.1	7.2	8.2	5.4	9.8	
AA TAX-EXEMPT LONG-TERM	AVG	1910.1	15	No load	0.38	18.6	7.1	8.4	5.9	25.7	
AA TAX-EXEMPT SHORT-TERM	▲▲▲	776.6	–4	No load	0.42	8.1	4.8	5.6	4.7	2.8	
AA VA BOND	AVG	263.5	22	No load	0.50	17.1	7.3	8.4	5.7	21.9	
LUE LINE TAX-EXEMPT HIGH-YIELD	▼▼	232.8	3	No load	0.61	16.7	6.6	7.9	5.0	13.5	
N KAMPEN AMER. CAP. CA INS. T/F A (ddd)	▼▼	146.9	13	3.25	0.78†	18.2	7.3	8.4	5.0	17.4	
N KAMPEN AMER. CAP. HI-YLD. MUNI A (eee)	▲▲▲	515.9	23	4.75‡	1.02†	13.9	7.9	8.7	6.6	20.2	
N KAMPEN AMER. CAP. INS. T/F A (fff)	▼▼▼	1361.6	23	4.75	0.88†	17.5	7.3	8.4	5.3	19.0	
N KAMPEN AMER. CAP. MUNI INC. A (ggg)	▼	823.8	66	4.75	0.99†	15.6	6.7	8.7	5.7	19.4	
N KAMPEN AMER. CAP. PA T/F INC. A (hhh)	▼	226.1	11	4.65	0.82†	16.6	7.6	8.9	5.4	20.0	

ncludes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
) Formerly Putnam MA Tax Exempt Income II A. (aaa) Formerly Putnam MI Tax Exempt Income II A. (bbb) Formerly Putnam OH Tax Exempt Income II A. (ccc) Formerly MetLife-State St
search Tax-Exmpt A. (ddd) Formerly Van Kampen Merritt CA Insured T/F A. (eee) Formerly American Capital Tax-Exempt H/Y MuniA. (fff) Formerly Van Kampen Merritt Insured T/F Inc A.
g) Formerly Van Kampen Merritt Municipal Income A. (hhh) Formerly Van Kampen Merritt PA Tax-Free Inc A.

DATA: MORNINGSTAR, INC., CHICAGO, IL

MUTUAL FUND SCOREBOARD

	RATING	SIZE		FEES		PERFORMANCE			PORTFOLIO		TREND
		ASSETS $MIL.	% CHG. 1994-95	SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%) 1 YR.	3 YR.	5 YR.	YIELD (%)	MATURITY (YEARS)	5-YEAR ANALYSIS
VAN KAMPEN AMER. CAP. T/F HI-INC. A (iii)	♦	664.1	10	4.75	0.87†	15.6	8.4	6.7	6.4	20.1	
VANGUARD CA TAX-FREE INS. INTERM.		213.9	93	No load	0.19	13.1			4.9	7.0	
VANGUARD CA TAX-FREE INS. LONG-TERM	♦	985.5	19	No load	0.19	18.6	8.1	8.9	5.3	14.3	
VANGUARD FL INSURED TAX-FREE		483.5	47	No load	0.22	17.7	8.4		5.0	10.3	
VANGUARD MUNI BOND HIGH-YIELD	AVG	1988.1	26	No load	0.21	18.1	8.1	9.8	5.7	11.9	
VANGUARD MUNI BOND INSURED L/T	♦	2017.3	16	No load	0.21	18.6	8.2	9.2	5.3	12.3	
VANGUARD MUNI BOND INTERM.-TERM	♦♦	5770.1	26	No load	0.21	13.6	7.5	8.7	5.0	7.3	
VANGUARD MUNI BOND LIMITED-TERM	♦♦♦	1683.1	3	No load	0.21	8.6	4.9	6.1	4.5	3.1	
VANGUARD MUNI BOND LONG-TERM	♦	1114.4	21	No load	0.21	18.7	8.3	9.5	5.4	14.5	
VANGUARD MUNI BOND SHORT-TERM	♦♦♦	1410.0	–4	No load	0.21	6.0	3.8	4.7	3.9	1.3	
VANGUARD NJ TAX-FREE INSURED L/T	♦	803.1	23	No load	0.21	17.3	8.0	8.9	5.2	10.8	
VANGUARD NY INSURED TAX-FREE	AVG	870.3	25	No load	0.22	17.7	7.9	9.2	5.2	11.3	
VANGUARD OH TAX-FREE INSURED L/T	AVG	198.6	35	No load	0.23	16.9	7.7	8.9	5.2	8.8	
VANGUARD PA TAX-FREE INSURED L/T	♦	1582.8	22	No load	0.20	16.5	7.8	9.2	5.4	9.2	
VOYAGEUR AZ INSURED TAX-FREE A		238.1	3	4.75	0.72†	19.1	7.5		5.0	16.1	
VOYAGEUR CO TAX-FREE A	♦	396.7	12	3.75	0.66†	20.5	7.6	8.8	5.0	21.8	
VOYAGEUR FL INSURED TAX-FREE A		242.4	1	4.75	0.20†	21.2	7.7		5.1	18.6	
VOYAGEUR MN INSURED A	AVG	307.7	8	4.75	0.61†	17.5	7.2	8.3	5.0	18.0	
VOYAGEUR MN TAX-FREE A	♦	455.2	12	4.75	0.90†	17.5	7.3	8.2	5.1	20.2	
WILLIAM PENN PA TAX-FREE INCOME	♦♦	123.5	35	4.75	0.79†	16.7	7.2	8.2	5.7	9.9	
INTERNATIONAL											
ALLIANCE NORTH AMER. GOVT. INC. B		1199.4	4	3.00**	2.41†	29.6	1.8		12.4	10.4	
ALLIANCE SHORT-TERM MULTI-MKT. B	♦♦♦	490.6	–38	3.00**	1.85†	4.5	0.4	1.9	8.8	1.2	
BENHAM EUROPEAN GOVERNMENT BOND		252.3	30	No load	0.86	24.4	13.2		7.5	6.6	
BLANCHARD SHORT-TERM GLOBAL INC.		181.8	–41	No load	1.51†	7.0	3.5		5.6	2.6	
CAPITAL WORLD BOND	♦♦	698.4	24	4.75	1.12†	21.4	11.8	10.2	7.0	9.1	
DEAN WITTER WORLD WIDE INCOME	♦♦♦	134.5	–18	5.00**	1.91†	18.2	7.5	5.3	8.9	6.3	
EV MARATHON STRATEGIC INCOME (jjj)	♦♦♦	144.7	–31	3.00**	2.00†	14.4	6.3	5.3	7.9		
FEDERATED INTERNATIONAL INCOME A (kkk)		170.1	–14	4.50	1.30†	17.5	12.5		7.7	6.8	
FIDELITY GLOBAL BOND	♦♦♦	196.2	–49	No load	1.14	6.7	2.9	4.9	5.8	7.8	
FIDELITY NEW MARKETS INCOME		173.5	–3	No load	1.28	8.0			9.2	14.3	
FIDELITY SHORT-TERM WORLD INCOME		122.0	–54	No load	1.01	7.8	4.5		6.3	2.0	
FRANKLIN GLOBAL GOVT. INCOME I	♦♦♦	158.0	–11	4.25	0.89†	18.1	8.9	8.0	8.1	8.8	
FRANKLIN TEMPLETON HARD CURRENCY	♦♦♦	127.3	116	3.00	1.17†	6.6	8.5	7.2	5.6	0.2	
G.T. GLOBAL GOVERNMENT INC. A	♦♦♦	356.1	–22	4.75	1.33†	15.6	7.7	7.7	6.5	7.3	
G.T. GLOBAL HIGH-INCOME B		223.0	6	5.00**	2.44†	19.3	13.0		8.3	16.1	
G.T. GLOBAL STRATEGIC INCOME B		362.9	–10	5.00**	2.15†	16.3	9.4		7.2	14.3	
GOLDMAN SACHS GLOBAL INCOME A		237.1	–32	4.50	1.28†	17.8	7.9		11.2		
IDS GLOBAL BOND A	♦♦	583.6	30	5.00	1.26	19.4	10.2	10.8	6.8	11.1	
LEGG MASON GLOBAL GOVERNMENT		146.4	1	No load	1.30†	21.1			11.2	6.6	
LORD ABBETT GLOBAL INCOME	♦♦	238.3	–4	4.75	1.02†	18.4	8.2	8.9	8.1	9.3	
MERRILL LYNCH GLOBAL BOND B	♦♦	540.9	–23	4.00**	1.61†	12.5	5.8	7.7	5.4		
MERRILL LYNCH SHORT-TERM GLOBAL INC. B	♦♦♦	371.2	–42	4.00**	1.52†	6.3	2.9	2.4	6.0		
MFS WORLD GOVERNMENTS A	♦♦♦	338.1	–6	4.75	1.54†	15.5	8.5	8.0	14.3		
PAINEWEBBER GLOBAL INCOME A		625.8	8	4.00	1.17†	13.2	7.5		7.0	5.6	
T. ROWE PRICE INTL. BOND	♦♦♦	1015.8	38	No load	0.98	20.3	12.3	11.3	5.9	7.8	
PRUDENTIAL GLOBAL LIMITED MAT. B (lll)	♦♦	111.8	–32	3.00**	1.97†	8.3	3.3	3.6	6.0		
PRUDENTIAL INTERM. GLOBAL INC. A	♦♦	182.3	–12	3.00	1.46†	23.2	9.9	8.1	5.1	8.4	
PUTNAM GLOBAL GOVERNMENTAL INC. A	♦♦♦	368.9	–14	4.75	1.27†	15.9	5.8	7.4	6.1	11.4	
SCUDDER EMERGING MARKETS INCOME		188.8	111	No load	1.50	19.5			10.3	13.0	
SCUDDER GLOBAL BOND (mmm)		335.0	–33	No load	1.00	7.7	4.4		7.5	2.6	
SCUDDER INTERNATIONAL BOND	♦♦♦	736.4	–32	No load	1.30	8.5	4.7	8.6	7.4	6.4	
SMITH BARNEY GLOBAL GOVT. BOND A		120.6	68	4.50	1.32†	15.4	9.7		6.5		
STANDISH GLOBAL FIXED-INCOME		134.5	–1	No load	0.65	18.1			8.5	10.0	
TCW/DW NORTH AMERICAN GOVT. INC.		613.1	–30	No load	1.52†	16.0	1.9		7.6		
TEMPLETON INCOME I	♦♦	194.9	–2	4.25	1.18†	18.2	7.9	8.3	6.1	6.9	
VAN ECK GLOBAL INCOME A	♦♦♦	111.6	–19	4.75	1.39†	17.3	6.1	6.7	6.0	5.5	
VAN KAMPEN AMER. CAP. GLOBAL GOVT. B (nnn)		109.6	–14	4.00**	2.18†	13.2	6.5		6.0		
WESTERN ASSET INTERNATIONAL SEC.		218.1	29	No load	0.30	13.9			5.8		
CONVERTIBLE											
BOND FUND FOR GROWTH A	♦♦	238.0	92	3.25	1.66†	26.0	14.7	20.6	5.9	7.8	
DEAN WITTER CONVERTIBLE	♦♦	201.7	15	5.00**	1.96†	20.6	10.7	12.9	4.9		
FIDELITY CONVERTIBLE SECURITIES	♦	1045.7	17	No load	0.85	19.4	11.4	18.5	4.3		
MAINSTAY CONVERTIBLE B	♦♦	426.0	136	5.00**	1.90†	22.6	14.6	20.4	3.4	8.1	
PACIFIC HORIZON CAPITAL INCOME	♦	233.9	17	4.50	0.97	24.1	12.8	19.2	4.4	8.5	
PHOENIX CONVERTIBLE A	♦	227.0	7	4.75	1.14†	21.6	8.7	10.4	5.2		
PUTNAM CONVERTIBLE INCOME GRTH. A	♦	789.5	18	5.75	1.16†	23.8	12.4	17.4	4.9	9.5	
VAN KAMPEN AMER. CAP. HARBOR A (ooo)	♦♦	393.8	6	5.75	1.04†	22.5	9.2	11.9	4.5		

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
(iii) Formerly Van Kampen Merritt Tax-Fr High-Inc A. (jjj) Formerly EV Marathon Short-Term Strat Income. (kkk) Formerly International Income A. (lll) Formerly Prudential Short-Term Global Income B. (mmm) Formerly Scudder Short-Term Global Income. (nnn) Formerly American Capital Global Govt Secs B. (ooo) Formerly American Capital Harbor A.

DATA: MORNINGSTAR, INC., CHICAGO, IL

UTUAL FUND SCOREBOARD

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dvance Capital I Group	345-4783	MI	313-350-8543
IM Family of Funds	347-1919	TX	713-626-1919
liance Capital Group	227-4618	NJ	201-319-4000
nerican Funds Group	421-4120	CA	213-486-9200
quila Group	872-5859	NY	212-697-6666
sset Management Fund (AMF)	527-3713	IL	312-644-3100
las Funds	933-2852		
bson Fund Group	422-2766	MO	816-471-5200
nham Group	331-8331	CA	415-965-4274
rnstein (Sanford C.) Fund		NY	212-756-4097
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anchard Group of Funds	922-7771	NY	212-779-7979
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nd Fund of America	See American Funds Group		
lifornia Investment Trust Group	225-8778	CA	415-398-2727
lvert Group	368-2748	MD	301-951-4820
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rdinal Group	848-7734	OH	800-282-9446
lonial Group	248-2828	MA	617-426-3750
lumbia Funds	547-1707	OR	503-222-3606
mmon Sense Trust	544-5445		
mposite Group of Funds	543-8072	WA	509-353-3550
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an Witter Funds	869-3863	NY	212-392-2550
laware Group	523-4640	PA	215-988-1333
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dge & Cox Group	621-3979		
eyfus Group	645-6561	NY	718-895-1206
pree Mutual Funds	866-0614	KY	606-254-7741
ton Vance Group	225-6265	MA	617-482-8260
npire Builder Group	845-8406	NY	212-309-8400
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delity Advisor Funds	522-7297	MA	617-439-6793
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st Priority Funds	433-2829		
gship Funds	227-4648	OH	800-354-7447
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Phoenix Funds	243-4361	CT	203-253-1000
PIMCo Advisors Funds	426-0107	CT	203-352-4900
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Virtus Funds	444-7123	VA	804-771-7131
Voyageur Funds	553-2143	MN	612-376-7000
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THE INTERNET

WHAT HATH YAHOO WROUGHT?

The Web is red hot, but guides to it are even hotter

It's a jungle out there on the World Wide Web—a wild, exploding tangle of home pages, hotlinks, and way cool sites. And it's a wonder that cyberspace explorers don't all get lost. As of Jan. 1, the Web included some 200,000 sites, or Web servers, that offered close to 20 million pages of information for public consumption. Dozens of times a second, all across the globe, the Web sprouts yet another new page of text, graphics, sound, or video, and the online trove expands by who knows how many more megabytes.

No wonder some of the most successful companies on the Internet are those that are helping masses of people find their way in this teeming overgrowth of information. Their so-called Web-search engines, which maintain free, public directories of the Net's sprawling contents, are among the biggest attractions on the Web and as a result, the most densely packed with paid advertising from companies such as Honda, Saturn, and AT&T.

A handful of companies—including InfoSeek, Lycos, Yahoo, and Architext—are leading the way. Their software robots, known as spiders or crawlers (box), work overtime to scan the Web, find every page there, and update their master indexes. Then, they can search those indexes in a flash, locating in mere seconds a page that might otherwise take hours to find on one's own.

PINPOINT PITCHES. How popular are these index services? Measuring audience attention on the Net is difficult. But market pioneer Yahoo! Corp. figures that every day, about 1 million people take 7 million peeks at Web pages from its directory. And over the course of a month, 3.5 million individuals browse. InfoSeek Corp.'s search engine is responding to about 7 million inquiries a day, says Robin Johnson, president and CEO. And Digital Equipment Corp.'s new Alta Vista engine, switched on Dec. 15 to show off the speed of DEC's Alpha 8400 computers, already gets 3 million "hits" a day.

Even though one person may generate a half-dozen of those daily hits, numbers like these are making advertisers' eyes bulge. And selling slivers of ad space on their directory pages—for fees of about 2¢ per audience impression—is exactly how the Web-indexing companies plan to make their money. Only Yahoo says it's profitable, but the others are likely to follow it into the black quickly. Webwide advertising revenues will grow from about $37 million last year to as much as $700 million in 1998, according to market researcher Forrester Research Inc.

One major driver of that growth: On the Web, advertisers can pinpoint marketing messages to individual viewers instead of using the mass media's shotgun approach. Using software from FocaLink, Broadvision, or Net Gravity, a Web server can match the types of ads it shows each visitor to his or her specific interests or consumer profile. It might show a frequent traveler a series of airline ads, for instan

Web-search engines, of course, a the ideal place to learn about a W surfer's particular interests. Every ti you visit an index site, you leave a tr of keywords and categories you sel from lists of subjects. The adverti may not learn your name but it can

TEACHING 'ROBOTS' A BIT OF NETIQUETTE

A robot may not injure a human being.
A robot must obey orders from humans.
A robot must protect its own existence.

Isaac Asimov wrote these "Three Laws of Robotics" half a century ago. Today, they are widely followed—but not as the sci-fi visionary anticipated. Computer scientists now use the word "robot" to describe computer search engines such as Lycos and Yahoo, which tirelessly index the World Wide Web. And inspired partly by Asimov's laws, folks who run these search engines have adopted voluntary guidelines to keep robots from running amok in cyberspace.

It's a good thing. The powerful searching programs they use—known variously as "robots," "spiders," "crawlers"—must update their d bases by repeatedly querying W around the world. But an uninte blizzard of queries from one rob be enough to swamp a small se

Martijn Koster, a software en at America Online Inc.'s Webcr Project, spotlighted this proble while working for a British net services company called Nexor Drawing on input from the Inte community, he developed rules ware robots. They include rest on how much time robots can li a site and how often they can v Koster also wrote standard me that Webmasters can post at th

seful profile of who you are. For ed revenue, the search companies also collect masses of consumer data sell it, in aggregated form, to adver- 's and others.

ow, the race is on to build stronger d names in what's shaping up as a y contested Web-searching market.

Yahoo remains the company to beat. First to market, it's already turning profits from selling spots on its pages to more than 50 advertisers

CO-FOUNDERS YANG AND FILO ASKED THEIR WEB VISITORS FOR SUGGESTIONS

At the start, the search companies seemed nearly identical, sharing similar origins and offering essentially the same service for the same price—free. Stanford University students started Yahoo and Architext Software Inc., two archetypal garage Internet startups that landed backing from blue chip Silicon Valley venture capitalists. Lycos is commercializing a search technology developed by chief scientist Michael L. Mauldin and other co-founders who used to work at Carnegie-Mellon University.

The main challenge is differentiating one search service from the others. At first, the contest was mainly over technical bragging rights—namely, search speed and index size. InfoSeek, for instance, started out last year by trumpeting an index that covered not just the Web but also several news wires and the Internet's 10,000-plus bulletin boards—smut, flame wars, and all. With an index covering 19 million Web pages, Lycos Inc. has claimed the world's largest and fastest Web directory.

The emphasis now is shifting from statistics on speed and sites covered to features that may be more meaningful to ordinary consumers. That means adding features to "build a branded consumer experience," says Joe Kraus, president and CEO of Architext. InfoSeek, for example, has added programming to its engine that periodically scans various data sources for information on any topics a customer chooses and automatically prepares a summary in the form of a customized Web page.

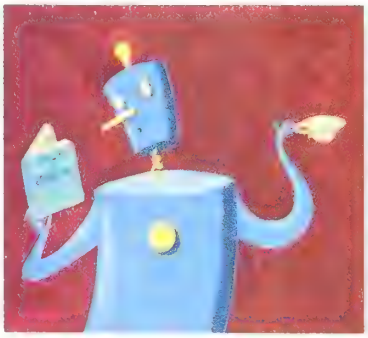
At the same time, the search companies are doing a lot more work on combing Web sites to preselect the most appealing ones. Architext has hired 30 journalists who have reviewed 51,000 Web sites so far. And the company has just acquired City.Net, a startup that creates Web sites for local and regional markets. Lycos has bought Point Communications, a Web-site rating service. And the McKinley Group Inc., a publishing company founded by Isabel Maxwell, daughter of the late British newspaper magnate Robert Maxwell, is not even offering a full-blown search engine. It's selling ads on a server that offers reviews of 40,000 Web sites.

The company to beat remains Yahoo—the first to market and backed by roughly $6 million in venture capital. It's already turning profits from selling spots on its pages to more than 50 advertisers, and it boasts one of the strongest brand names in cyberspace. It started out in April, 1994, after its founders, Jerry Yang and David Filo,

; which directories are off-lim- search services obey these the grass" signs, says Lycos' ıtist Michael Mauldin. this ad hoc fix has been effec- reason: only a ge robots g to index "The huge required ıe minor says David , chairman iversity of software- ıg pro- lear Lake. could get hairy if Web-search- ts more deep-pocketed com- media giants and rising com- rains collegiality. More are programs to let individu- their own robots. One such program, called Fish, is already available for free on the Net. Built as an enhancement of the Mosaic program that Netscape Communications Corp. adapted as its Web browser, it appeals mainly to software engineers. But bundled in a user-friendly package, Fish would let millions of PC users set up their own mini-bots. "It would be like everyone deciding to get off of the public transportation system and drive to work," says Mauldin. "The overall structure of the Internet couldn't handle it."

Further down the road, there could be an explosion of intelligent "agents" that not only collect data for individuals but also analyze the data. That will almost certainly add to network congestion. Some experts, such as University of Washington computer-science professor Oren Etzioni, predict that smarter robots will conduct more rational searches, reducing the strain. Still, robots may soon find themselves idling on increasingly busy network arteries where, like humans caught in traffic jams, they may find it difficult to behave politely.

By Neil Gross in New York



TO BE ACCEPTED IN WEB SOCIETY, A ROBOT SHOULD:

1. Identify itself when it approaches a Web site
2. Obey a set of rules called the Robot Exclusion Standard
3. Observe the wishes of the site administrator
4. Limit the number of queries addressed to any given site
5. Limit the frequency of visits to each site

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recognized the growing popularity their informal listings of Web sites. F soliciting suggestions from all Web su ers and adopting a hip 'tude and jaz graphics, Yahoo quickly grew into one the Web's hottest spots—and a maj inspiration to the entrepreneurs no chasing it.

Competition has forced Yahoo to ad full-Web searching, but it still emphas es the judgment that goes into its dire tories. "What's really important to t audience is that they get high-quali results back, not how the results a generated," says Tim A. Koogle, pre dent and CEO. With Ziff-Davis Publis ing Co., a leading publisher of comput magazines and an investor in Yaho the company is developing *Yahoo Int net Life*, a print and online magazi

BATTLE OF THE SEARCH ENGINES

ALTAVISTA.DIGITAL.COM A speedy index site that shows off Digital Equipment's Alpha computers

WWW.EXCITE.COM Emphasizes strong editorial content and regional listings

WWW.INFOSEEK.COM Indexes the Web, news wires, and other electronic media

WWW.LYCOS.COM Focus is on maintaining the largest Web index

WWW.YAHOO.COM First to market, strong branding strategy

Yahoo is also working on a Japane language search site with Softbank, t Japanese computer distributor and tra show operator that owns Ziff-Davis a has a stake in Yahoo. Yahoo offici won't comment, but Wall Street expe Yahoo to be the first company in t category to go public.

One thing Web-search companies c count on is increasing demand. As m economic activity pours into cyberspa from publishing to retailing and cor rate purchasing, people will need h finding their way. Search products rapidly proliferating: Frontier Techno gies offers Lycos' Web index on a ROM disk, for off-line use. Quarterde Inc. and Blue Squirrel Inc. offer p sonal computer programs that bro cast a single query to multiple Web gines and merge the results in listing. And a company called quiry.com in San Mateo, Calif., launched a Web-search engine just computer professionals. With more t 30 commercial and academic search gines already prowling the Web, day we may need a search engine j to find the right search engine.

By John W. Verity in New York, w bureau reports

TED BY OTIS PORT

IIPS STEEPED JAVA

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.'s hot new computer
guage for writing pro-
ums that users can run
er networks—there's a
problem: Java pro-
ums are about as
edy as molasses in
uary. That's because
software instructions
not compatible with
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Sun's solution: dedicat-
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y take until late 1997.
reover, since the chips
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a programs, they'll be
less unless Java and
related operating sys-
become a success and
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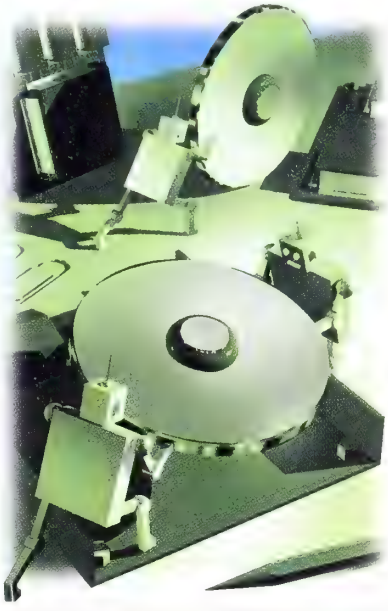
grams—and that's far
n a sure thing.

MANUFACTURED IN MUNCHKIN-LAND

IT COULD BE A FACTORY SCENE FROM *TOY STORY*. BUT THE tiny factories being built by scientists at Carnegie Mellon University are small only in scale. They're designed to do big-time work—and generate fat payoffs.

Roughly the size of a table top, the little factories will have teams of fast-working, sharp-eyed minirobots scurrying about. Their first job: to assemble computer disk drives. If all goes well, CMU hopes armies of fistsize robots in tiny, portable factories will take on a wide variety of precision-assembly jobs currently performed by workers and larger robots.



The National Science Foundation-funded project also aims to speed up the design and deployment of automated assembly systems. CMU researchers will build the robots with modular parts and design them with far-flung suppliers through the Internet. Researchers hope this will let them design, build, and deploy automated assembly systems in less than a week, down from four weeks now, while increasing accuracy. The lessons learned with these robots will smooth the way for ever-smaller machines.

WILL A GENE-ALTERED MITE MAKE RIGHT?

THE NEXT LANDMARK IN the area of genetically altered species may come from the University of Florida. UF entomologist Marjorie Hoy is awaiting permission from the U.S. Agriculture Dept. to field-test a tiny, flightless mite called *Metaseiulus occidentalis*, into which she has inserted a bacterial gene marker. After the insertion, the mite was bred for 300 generations—about three years. If the USDA consents, it will be the first genetically altered arthropod ever released into the environment.

M. occidentalis preys on its cousin, the spider mite, which ravages strawberries and ornamental plants in Florida.

Since the mite is native to the Western U.S., Hoy wants to genetically alter it for Florida's climate. But first she wants to demonstrate the safety and viability of the genetic-alteration method. This first bacterial marker won't actually change the mites' biological traits—just provide a way for them to be identified. Therefore, Hoy says, the experiment poses no risk to the environment.

'HOUSTON, WE HAVE A PROBLEM—NO CHIVES'

SOMEHOW IT DOESN'T FIT THE image of the Space Age, but the latest in high-orbit sustenance and climate control may be the potato. Or the wheat plant. NASA researchers are experimenting with growing both crops in space to feed crews, provide oxygen, and purify water. At the Kennedy Space Center, potatoes grown in a 20-foot-long cylinder produced four to five times the oxygen required for a mission, as well as over half the food required for one crew member. They also provided enough drinking water for four astronauts by absorbing waste- water through their roots and respiring clean water vapor from their leaves. The Johnson Space Center has conducted similar experiments with wheat.

Lofted into orbit aboard the shuttle Columbia last October, five potato plants produced perfect spuds in spite of the near-zero gravity, says University of Wisconsin botanist Judith G. Croxdale. The potatoes contained large protein crystals, she says. To keep the water from flying around, the plants' roots were sealed in a chamber, with just a small hole for the stem. Cosmonauts encountered technical difficulties last year growing wheat aboard the Mir space station. If the astronauts get bored, they could always start up a nice little distillery.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwfeb@businessweek.com

SEMICONDUCTORS

THIS ONLY HAPPENS TWICE IN A LIFETIME

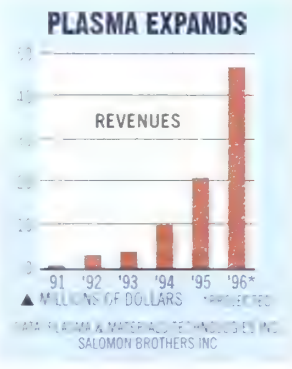
John Rollwagen sees the spirit of Cray in a chip upstart

Moments after John A. Rollwagen and Gregor A. Campbell first shook hands in October, 1993, both sensed something special. "We just really clicked," says Rollwagen, longtime CEO of supercomputer maker Cray Research Inc.

Rollwagen had reluctantly journeyed 2,000 miles from St. Paul, Minn., to Chatsworth, Calif., to inspect Campbell's company, Plasma & Materials Technologies Inc., and perhaps join the board. Rollwagen wasn't keen on that idea. He was still recovering from his four-month fling in Washington. President Clinton had asked him to be Deputy Secretary of Commerce, which meant resigning from Cray. But he left the Administration after only four months when the Securities & Exchange Commission began looking into Cray's stock trading. So he decided to work off his sense of civic duty by helping small companies, including those affiliated with St. Paul Venture Capital Inc., a backer of PMT's patented technology for generating a charged gas, or plasma, to process silicon wafers into chips.

Campbell jumped to attention when he heard of Rollwagen's availability. Campbell had gotten hooked on Cray supercomputers in the mid-1980s while he was earning a PhD in plasma physics from the University of California at Los Angeles. "And because I knew nothing about business when I started PMT, I read voraciously—especially a *Harvard Business Review* article" that analyzed Cray's early success. As a result, Cray became a model for launching PMT. And the topper would be getting Rollwagen to join the company. That would also give a tiny startup like PMT more credibility when the time was ripe for a stock offering.

CAMPBELL AND ROLLWAGEN: *Their etchers could change chipmaking*



Evidently Campbell's imitation of Cray succeeded better than he knew. "PMT reminded me so much of Cray in the 1970s that it was spooky," says Rollwagen. In particular, he saw parallels with PMT's unique technology and ambitious growth strategy. "I was attracted ... Greg's aggressive, take-no-prisone... business plan—PMT is either going ... be big-leagues or nothing."

Because their first meeting went ... well, Campbell decided to ask Rollwag... to sign on as chairman, not just as a ... rector. Rollwagen said yes on the spot ... if he could continue living in St. P... and come to California once or twice ... month. "It's like I'm getting a seco... chance to relive my misspent youth ... and help Greg avoid the same mistak... I made." Like what? "That was just ... figure of speech—I ne... made any mistakes," ... says wryly. "That's ... mentor!" says Campb... who once wanted to o... up Mother Nature ... shaping a superhot pl... ma into a miniature s... even brighter than ... sun: a Tokamak fusi... energy reactor. Now, ... just wants to take on ... likes of Applied Mater... Inc., the world's top s... plier of chipmaking equ... ment, with sales last y... of $2 billion—100 times ... big as PMT's.

The idea for PMT ... sparked in the mid-19... when Campbell read h... the chip industry ... working on harness ... plasmas to scratch ... the circuit lines "print... on silicon. Traditiona... these lines are etc... with liquid acid. But ... etching eats out V-sha... grooves, so channels t... are wide enough at ... bottom have tops wider than necess... That means a chip's wispy circuit l... can't be packed together as tightly ... they should be as line widths shrin... 0.35 microns or less. Only a handfu... chipmakers are now at this point.

HUNTING FOR CAPITAL. Plasmas can ... el out U-shaped grooves with ne... vertical sides. Negatively charged ... rain down from the plasma, pulled ... positive charge in the wafer. In indu... a decade ago, this was a novel appro... But to fusion researchers, plasmas w... old-hat. So Campbell and his UCLA ... adviser, Robert W. Conn, cooked u... system exceeding the chip industr... wish-list specifications—and went h... ing for venture capital.

They bumped into a wall. "The ... [venture capital] guys said we'd n... break into the semiconductor equipm...

siness," recalls Campbell. Chip compas just wouldn't risk buying such a piece of equipment from an upstart. t Japan's suppliers reacted positively. late 1991 and early 1992, Campbell li- ised the technology to Canon Inc. l NEC Corp., and then "the VCS reall I we had a tiger by the tail."

Despite its impressive jump to $21.3 lion last year, double its 1994 sales art), PMT is still running uphill. ey've got good technology," says Cal- Y. Chang, an industry analyst at rket researcher Dataquest Inc., "but ir market share is tiny—less than 1% ast year's $2.5 billion etch market."

While PMT has sold systems for up $2.8 million each to such major chipkers as Toshiba, Samsung, and LG nicon, most sales have been one-shot ls for evaluation. Rebecca Gale, a elopment manager at Texas Instruits Inc., says she is impressed with PMT machine, but TI isn't apt to buy e until it's confident PMT can crank m out in volume and provide global rice. Campbell figures the $40 million y from last August's initial stock ofng will provide staying power—and funding for joint efforts with NEC LG Semicon (formerly Goldstar niconductor Ltd.) to apply PMT's techogy to other types of chipmaking ipment. (After running up to $22, res are now trading a couple of its below the original $14 price.)

LEAGUE BID. Meanwhile, Dallas Semiductor Corp., the first company to a PMT etcher into actual production, taken delivery of its second sys—and will buy more as the need es, says Senior Vice-President Chao Mai. But Dataquest's Chang says PMT 't be in the big leagues until it gets order for 30 or 40 etchers from a e chipmaker. Even small chip plants cally have a dozen or more etchers. Unless multiple-machine sales start ng in soon, PMT could lose its techgy edge, warns G. Dan Hutcheson, sident of chipwatcher VLSI Research "They started out ahead of the , but the other etch guys are now hing up."

Rollwagen knows things are going to even tougher. That's why he has dily increased the time he devotes PMT—to 35% in 1994 and 50% in . "Next, we're going to get him to e out here full-time," predicts pbell. But first PMT needs another people to handle the expected surge ales. "That's like Cray, too—I hope," Rollwagen. "We had 100 people n we went public, and five years r it was 1,000." As a shareholder in company, Rollwagen's reward could out to be more than nostalgic.

By Otis Port in New York

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EXECUTIVE SUITE

CATHY ABBOTT IS NO GOOD OL' BOY

The former Energy wonk brings new blood to Columbia Gas

Other energy executives may be able to brag about gold cups won at golf tournaments, but Catherine Good Abbott can point to a really special trophy. A few years ago, she haggled for days with a New Mexico gas producer when her employer, Enron Corp.'s big Transwestern Pipeline Co., wanted to renegotiate a contract because of sliding prices. "I got to be the bad guy," she recalls. The producer decided to memorialize her by christening a new well with the nickname he had taken to calling her. Abbott still speaks proudly of "Hard-as-Nails No. 1" in Chaves County, N. M.

While the well failed, few things Abbott has undertaken in 18 years in the industry have been washouts. Now Abbott is tackling her biggest job yet. As the new chief executive of two key subsidiaries of Columbia Gas System Inc., she is taking charge of a $1-billion-a-year natural gas pipeline network even as the once highly regulated industry grapples with unfettered competition. What's more, Columbia is rebuilding after four years in Chapter 11.

Abbott started out in Washington, as an Environmental Protection Agency numbers-cruncher whose analyses for the Carter White House helped launch deregulation. Then, she jumped to a trade group, the Interstate natural Gas Assn., as a policy analyst. Eleven years ago, she moved to Houston as a vice-president of Enron, where she marketed gas nationwide. Last spring, she left to consult for companies including Columbia. But when Oliver G. Richard III, who took the helm of Columbia Gas System last April, offered her the $300,000-a-year post late last year, she jumped at it.

The job—CEO of two units that account for one-third of Columbia's sales and more than half its profits—makes Abbott one of a handful of top female executives in the natural gas industry. Her rise, insiders say, is a sign of how the industry's old utility-like, engineer-dominated culture is giving way to c where marketing, dealmaking, and nancial innovation reign. Says Richa who knew Abbott when he was a De ocratic senator's aide and later a Fed al Energy Regulatory commission "It's a time for change in our busine It's a time to make a difference, a it's a time to have new leadership. S represents all those things." No James V. Walzel, a friend who cha Houston's HNG Storage Co.: "Deregu tion has moved out a lot of old-time who were all men." And while tra of the good-ol'-boy network linger, s Rebecca A. McDonald, president Amoco Corp.'s natural gas group, " good ol' boys respect performance."

NO IDEOLOGUE. Abbott has always bee high performer. The brainy daughter biochemist and a math professor, she tered Swarthmore College as a m and science major in 1968. Interested becoming a minister, she switched major to religion and sp two years working fo program that develo Sunday school curriculu Idealistic about government, she hea to Harvard University's John F. Kenn School for a master's in public pol From there she joined the EPA.

In Washington, she impressed f and friends with her passionate but r ideological advocacy. "Any discomfo cause has more to do with my perso ity and style than the fact that I a woman," she says. Colleagues recall getting fired up over such arcane cepts as incremental pricing. "Meek

CATHERINE GOOD ABBOTT

TITLE CEO, Columbia Gas Transmission and Columbia Gulf Transmission—interstate pipeline subsidiaries of Columbia Gas System, with revenues of more than $1 billion

AGE 45

EDUCATION MA, Harvard University's John F. Kennedy School; BA, Swarthmore College

CAREER 1976-1982 Worked for the Environmental Protection Agency, President Carter's Office of Energy Policy & Planning, and the Energy Dept.

1982-85 Vice-president, Interstate Natural Gas Assn.

1985-95 Vice-president, Enron

1995-January, 1996 Principal, Gem Energy Consulting

FLEXIBLE FLYER: *Abbott helped deregulate the natural gas industry*

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Cathy Abbott don't go together in the same sentence," says Benjamin Schlesinger, a Bethesda (Md.)-based consultant and ex-Energy Dept. official. "She was a brilliant analyst who could explain a problem and get her point across."

Not that she was always right: She once argued that after deregulation, natural gas prices would soar to meet oil prices. Instead, prices for both collapsed in a mid-1980s glut. It was rock-bottom prices, along with long-term, high-price contracts with producers, that landed Columbia in Chapter 11 bankruptcy in 1991. It emerged last November.

Now, Abbott will guide a $400 million pipeline expansion to get Columbia caught up with rival pipelines that grew during those four years. She'll also lobby Washington for more reform in areas where regulation lingers. Among her 3,600 employees, she'll have to deal with jitters about potential downsizing and relocation of the head office.

HANGING OUT. Despite such responsibilities, Abbott says family is her No. 1 priority. She married Ernest B. Abbott 22 years ago, and they've followed intertwined career paths, first at Harvard, then in Washington, and finally to the natural gas industry. A condition of her joining Enron in Houston was that Ernest, an attorney, find a good job. He now directs industry affairs at Tenneco Inc.'s energy division. Ernest says the two keep each other's business private, adding: "It's important, if you're the spouse of someone in a competing company, that you don't become an expert on that competing company."

Abbott insists she'll provide for plenty of "hanging-out time" with her two sons, Chris, 13, and Tim, 10. For years, family vacations have centered around hiking—in 1995, along part of the Appalachian trail. In a January fun run with the family, Abbott diplomatically crossed the finish line just behind Tim. But in the months ahead, Abbott will be spending weeknights in an apartment in Charleston, W. Va., where Columbia Gas Transmission is based. Eventually, its headquarters and Columbia's corporate headquarters in Wilmington, Del., may move, taking the Abbotts north. "We will all be in one place after the summer," she says, declining to say where.

A Democrat who moves easily among Republicans, a woman in a once macho industry, and a Marylander who warmed to Houston, Abbott says she has found flexibility essential. When she brought her direct, businesslike style to Texas, she jokes, she had to take "Southern lessons" from a friend. Now that she's a CEO, Hard-as-Nails Abbott may find those lessons in diplomacy invaluable.

By Joseph Weber in Philadephia, with Gary McWilliams in Houston

TAXES

NEW TOLLS ON THE INFO HIGHWAY?

States see big revenues in cyberspace

For cybernauts in Spokane, Wash., it was a rude awakening. On Jan. 15, revenue-hungry town officials proposed a 6% tax on gross receipts of Internet access providers. Spokane City Councilman Chris B. Anderson, a foe of burdensome business taxes, blew his stack. "This is a money grab on an embryonic industry that's only now becoming viable," he says. That afternoon, Anderson contacted local Net service companies to mount a defense, and one firm set up a Web site for users to blast the plan. The mayor's office and city council were flooded with E-mail and phone calls. Grassroots reaction was so strong Spokane decided to delay the new levy pending further study.

A happy ending? No, just the beginning. The Spokane eruption is likely to repeat itself in cities and states across the country as local treasurers increasingly eye online services as a new source of cash. Business on the Net has mushroomed from nil two years ago to an estimated $200 million today, and state and local tax collectors from Washington to Texas to Florida are trying to devise ways to make sure they don't lose tax revenue as commerce migrates from the real to the virtual world.

NOT SO FAST. "You can't ignore the growth of online communications," says Duston J. Jensen, tax manager of Spokane's cross-state rival, Tacoma, which recently was able to apply an existing telecommunications tax to its Internet-access providers. "The Net is here."

Not so fast, says the nascent online industry, which has grown explosively over the past two years amid little regulation. Company officials are outraged

at what they see as clumsy attempts to hobble cyberspace with ill-suited tax rules. The government has to be careful not to do "something that's g to kill this business," says Bruce J. F director of state taxes at Micro Corp. The industry argues that t would hurt the ability of startup get into electronic commerce. Beside says, states have no jurisdiction to most out-of-state commerce, much business in cyberspace, and manda online companies to remit sales t would be a logistical nightmare.

Still, the battle is already on. T tax officials issued an advisory to access providers last fall that they subject to the state's 1.4% telecomm cations tax. And a major test is loo in Florida. The Florida Revenue I had planned to extend an existing gross receipts tax and 7% sales t telecom services to Net access an mail services last September. But agency, flooded with complaints, de

THE TAXMAN COMES TO CYBERSPACE

State and local governments are considering new tolls on traffic in the online world.

MULTISTATE TAX COMMISSION This cross-state tax body is discussing model rules to extend state jurisdiction over online services.

FLORIDA The st commission has extending an exi com tax to cover and Internet-acc vices. Lawmaker soon take up the

old off until July 1 to allow the legture to consider the proposal. "This n important tax-policy issue that obsly will be affecting a growing numof businesses as more and more panies depend on computer telecomnications," says Revenue Dept. keswoman Donna O'Neal.

he online industry, meanwhile, is ring up to stop Florida and Texas before other states jump on the bandwagon. "States watch each other,"

explains McConnell, a manager at ral Electric Co. ort Myers, Fla. one state adses an issue, other states will, too." federal government isn't seeking to nd its taxation of online communica-, but it already imposes a 3% excise n users of telecom services, includnline and Net-access services.

line companies complain that city state efforts to shoehorn them into ing taxes—written largely for manuring businesses—unfairly penalthem. "A tax structure made les ago doesn't apply to the way o business today," fumes Carol L. , government-affairs director at the rmation Technology Assn., a com- industry group.

reover, collecting sales tax from mers in cyberspace can be daunting.

OUTRAGE

"This is a money grab on an embryonic industry," says one opponent of cybertaxes

Most real-world merchants occupy a physical location where sales taxes can be collected. But online marketers have a harder time pinpointing the geographical locale of their customers, who zap orders through cyberspace instead of paying for them in a store on Main Street.

In 1992, the U.S. Supreme Court ruled that states can tax direct marketers located out of state—such as Lands' End Inc. or L.L. Bean Inc.—only if the companies have a physical presence in that state, at least in the guise of a representative's office or service bureau. Online companies, such as America Online Inc., based in Vienna, Va., generally don't need such offices to sell services.

LOCATING CUSTOMERS. Some of these problems can be easily fixed, say state tax experts. Careful drafting can help avoid double taxation. And new technology—such as software announced last November by Netscape Communications Corp. and AVP Systems—can help cybermarketers locate the geographical addresses of their customers.

Even if the online companies do thwart the tax collectors in Washington, Texas, and Florida with legal challenges and deft lobbying, they still must contend with the Multistate Tax Commission, an advisory group of tax experts. The Washington-based commission is drafting model rules for state lawmakers to use in taxing online transactions. It's also soliciting the cooperation of the online industry so that guidelines fit the new technology. But says Paull Mines, general counsel at the MTC: "It's too significant a part of the economy to suggest there should be a long-term exemption from taxation."

Whatever model the commission devises, both sides expect it will be tested before the Supreme Court. The industry hopes local governments will recognize that a sympathetic tax policy might encourage growth of their economies. "Technology jobs will go to the states that are the most tax-friendly," says Bob Smith, executive director of the Interactive Services Assn., an online-services trade group. But as the online industry takes off, it's only a matter of time before the taxman comes calling.

By Catherine Yang in Washington

AND E, WASH. City in both municiave proposed sion of an existm tax to Inters services.

MASSACHUSETTS AND COLORADO Both states are studying taxing online communications and say they don't want to discourage tech growth in their economies.

TEXAS Net-access providers are subject to an existing telecom tax and online service providers to an information-services tax.

DATA BUSINESS WEEK

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EDITED BY AMY DUNKIN

CYBERSMUT: HOW TO LOCK OUT THE KIDS

Last fall, Robert Boisvert got a nasty surprise while cleaning out the hard disk on his PC. Sifting through the files, he came across Playmates of the Month for July, August, and September. "I know I didn't download them," says the China Lake (Calif.) father of five. "One photo can be an accident, but three months of centerfolds is no accident."

Boisvert determined that one of his teenage sons had fetched the images from *Playboy*'s World Wide Web site. But instead of trusting the kids not to prowl for porn, he turned to CyberPatrol from Micro-Systems Software, one of a burgeoning breed of software products that promise to help parents shelter their children while they cruise the wide-open Internet.

ONLINE

GOOD JUDGMENT. Parents can hardly be blamed for wanting to protect their children from raunchy, obscene, or even violent content on the Internet and commercial online services. While posturing politicians and others may have overstated the actual dangers, there's no question that kids can wander into areas where they don't belong. The good news is that access-control software, while far from perfect and no substitute for teaching good judgment, can at least reduce the potential for children getting into trouble. This software is primarily an Internet-only access tool. The online services have some filtering capacities for their own content, but less for Internet newsgroups accessed through them. They can't police Web sites.

CyberPatrol (Windows and Macintosh), CYBERsitter (Windows only), and SurfWatch (Windows and Mac) are all variations on the same theme: Each company compiles a list of objectionable Web sites and newsgroups and blocks access to them. A subscription to keep the list up to date, downloaded from the Internet, costs $5.95 a month for SurfWatch, $19.95 for six months for CyberPatrol, and is free for CYBERsitter.

The contents of the Internet change faster than frequent updates can track, so the programs supplement their bad-site list by watching for words or phrases in the names of sites or newsgroups. This filtering function can often produce curious results. All programs have enough built-in intelligence to avoid the kind of absurdity that hit America Online last year when it banned the word "breast" and cut off online discussions of breast cancer.

During a recent test, the programs gave access to pictures of a cut-up chicken titled "Big Breasts." CyberPatrol permitted, but SurfWatch blocked, access to a Web page called "Name the Breasts." It turned out to be a picture of a scantily clad Ted Kennedy; the software doesn't promise good taste. The programs barred entry to *Penthouse*'s explicit Web site, but not to a college student's page featuring nude photographs of herself.

SurfWatch allowed a search of the Web for sites discussing sex education but blocked any attempts to visit them. It also prevented reading the many sex-themed

Making the Internet Safe for Children

PRODUCT	SPECIAL FEATURES
CYBERPATROL, MICROSYSTEMS SOFTWARE $50	Parents can program hours of Internet time, and machine will automatically cut off access. Download demo version from Internet: http://www.microsys.com/
CYBERSITTER, SOLID OAK SOFTWARE $40	Allows most customization, offering choice of outright blocking, issuing a warning, or maintaining a log of access attempts. Download demo: http://www.solidoak.com/
NETNANNY, TROVE INVESTMENT $50	Most flexible: Software is not limited to Internet, works with all services. Download demo: http://www.netnanny.com/netnanny/
SURFWATCH, SURFWATCH SOFTWARE $50	Program is easiest to use of all options and worked flawlessly with the new Windows 95 operating system. Download demo: http://www.surfwatch.com/

DATA: COMPANY REPORTS

rsgroups but permitted kdoor access to some of n through archives on the). All three programs al- a parent in possession of assword to turn off the trols temporarily. But e of them lets you set dif- nt levels of control for erent children.

LIMITS. The programs er in the extent of cus- ization they allow. CYBER- r supplies a basic set of rs and bad sites but al- s parents to customize ngs to be stricter or loos- han the default. It also rs parents a choice be- en outright blocking of ac- to certain classes of , just issuing a warning n kids try it, or quietly ntaining a log of access mpts. CyberPatrol offers detailed customization adds a useful feature of wn: Parents can set lim- by time of day or total s, on when their kids can se the Net. Once the set is up, then CyberPatrol automatically cut off ac- to the Internet.

urfWatch has a different osophy. You can't cus- ze the configuration of current version, though pcoming revision will add options. But Jay Fried- marketing vice-president SurfWatch, says the com- decided to trade flexi- for simplicity of setup robustness of operation. ed, the Windows 95 ver- of SurfWatch was the product that worked essly with the new osoft operating system. other software products problems with installa- configuration and, in cases, interfered with net access.

etNanny (for Windows) a different means to a ar end. "We don't believe ing a censorship compa- says business develop- manager Graham Heal. believe in people mak- their own decisions." er than a list of pro- ed sites, NetNanny uses tionary of words and phrases. Parents download the dictionary then decide which words they want to edit out. Unlike the other products, NetNanny can monitor all non-Internet commercial online services such as America Online, bulletin boards, even access to files stored on the computer's hard disk. But it requires much more commitment from the grownups to set up the filtering. The NetNanny program is also tricky to install, especially on Windows 95.

If you don't already have Internet access, a couple of all-in-one products for Windows can get you started and build in access control at the same time. Internet in a Box for Kids from CompuServe ($50) combines Internet connectivity software and a special child-oriented version of the Spry Mosaic browser with SurfWatch. Unfortunately, it's quite hard to configure unless you arrange Internet service through CompuServe's sluggish InterServe network. For Windows 95 users, the $99 InterGO from TeacherSoft (214 424-7882) is a slick package that takes advantage of Win95's built-in networking to support a browser designed for children. InterGO seems particularly well-suited for use in schools.

Except for NetNanny, all of these programs are designed to restrict access only to the Internet, not to online services. In fact, they may not control access if you surf the net via America Online, CompuServe, or Prodigy. Whether or not the programs will work depends on how you connect with your online service; customer service should be able to give you the details.

Commercial online services provide some filtering features to give parents more control over how their children use the services. America Online allows parents to block access selectively to chat rooms, including conference and member-created rooms, news groups, and instant messages. Only the master account holder can use the parental controls that can be set individually for each of the up to five screen names on an account. Prodigy also allows individual options for each family member. CompuServe is the most limited: Users can block access to certain areas, but then all subscribers on the same account are restricted.

STANDARDS. If all of these arrangements sound ad hoc, that's because they have mostly sprung up in recent months in response to parental concerns and political pressures. The World Wide Web Consortium, the nearest thing the Web has to a governing body, is taking a more systematic approach. In about a month, it will issue the first standards for what's called the Platform for Internet Content Selection (PICS). The owners of Web sites will use the PICS standards to code their pages. And organizations such as the National Council of Parent Teacher Associations will create ratings standards. Access-control software could then use the combination of coding and ratings to decide who gets to see what. SafeSurf, a commercial operation, is also preparing its own third-party ratings of Web sites.

Some sense of order should be a welcome development. But no system of ratings or mechanical controls will, by itself, keep kids out of trouble. In the end, you'll face the challenge of parenting that long predates the Internet: Teach your children well. *Steve Wildstrom and Toddi Gutner*

Most of the programs tie Junior's hands on the Net–not on commercial online services

CREATE A BUSINESS PLAN—TO PASS ON THE WEALTH

Over the past 40 years, Edward and Allan Nierman spent countless hours and dollars turning their father's small plumbing-supply store into a company that generates $30 million a year in sales. With all of their assets firmly enmeshed in the Canton (Mass.) business, the brothers wanted to divvy up the inheritance pie equally among their six children—only one of whom works for the company—and also preserve the operation for future generations.

SMART MONEY

It's a growing problem. Demographics indicate that the greatest wealth transfer ever is about to take place in the U.S. Like the Niermans, many post-World War II entrepreneurs are nearing retirement and contemplating how to pass on the family business. Too often, the lack of an exit strategy leads to the firm's demise—two out of three family businesses never make it to the next generation. The key is to plan early and include the children in the process.

ONE BOSS? The biggest cause of failure is estate tax. "People are so committed to the search for equity that they overlook the impact of taxation and how it can undo a lifetime of work," says Howard Blank, president of Blank Financial Group in New York. That's because when the owner dies, the heirs are hit with inheritance taxes averaging 50% to 60%. The Internal Revenue Service allows nine months for the children to come up with the cash. If unprepared, they may be forced to sell the family business to cover the tax liability.

Even if the heavy weight of taxes doesn't cause the business to crumble, unforeseen events such as divorce, illness, or mismanagement might. Dividing the business equally when, as with the Niermans, only one of the children has contributed to the company's success can create serious conflict if the business is the owner's one source of equity, says Santa Monica (Calif.) attorney Jeffrey Condon, who co-authored *Beyond the Grave* (HarperCollins, $14) with his father and law partner, Gerald. Making one child the boss prevents operational gridlock but may ultimately strain family relations.

There are ways to keep the family happy and the business running, however. One innovative approach is to do what the Niermans did: Using a detailed buy-sell agreement, they recapitalized the company's stock into 10% voting and 90% nonvoting shares, explains Boston attorney Allan Landau. Each brother received half of the voting and nonvoting shares. When Allan Nierman retired, he gave his voting stock to Sheldon, his son in the company, and his nonvoting stock to his other two children. Because he was still working at the store, Edward kept his voting shares and made gifts of the nonvoting shares to his children.

When using these agreements, it's essential to spell out the specifics and anticipate future points of contention. Gerald Condon advises adding a dispute resolution clause just in case. Under the terms of the Niermans' agreement, five years after the death of both founders, Sheldon can call, or buy out, his siblings' and cousins' shares at a premium. Likewise, they have the right to "put it" to Sheldon and demand their stock be bought back at fair market value—two years after the deaths of Allan and Edward. If Sheldon does not have the cash needed to purchase their shares, he may use company funds to do so on an installment basis, making the interest tax-deductible.

By recapitalizing and giving away the stock long before their deaths, the owners freeze the estate's value. Therefore, the business will be taxed on its worth at t time the owners make t gift. "If you don't do th 50% of any future ga would be lost to estate tax So while the founders co tinue to grow the busine they're actually growi more tax, not more equit Blank says.

Treating the shares gifts reduces the estate's v ue further. Under curre tax law, each shareholo may give up to $10,000 t free to as many people as or she wishes. To ensu that the gifted shares s in the family, a smart mo is to do what Landau and place them in lifetime revocable trusts.

To further prot such an intric deal, consider tra ferring any fut liability to insurance c pany by tak out corpor life insura on the foun When the c er dies, the mo may be used to cov estate taxes, fund business, or pay out c hungry heirs. And nami lifetime irrevocable t both the designated ow and beneficiary of the p will help the heirs a onerous estate taxes. premium cost is split tween the company and irrevocable trust. But member: The earlier you the lower the cost. At 60, average premiums run about 2% annually o principal to be insured age 75, they jump to This may sound pricey when the owner dies money goes into the free from estate tax. A something unexpected pens that mucks up plans, you're protected.

Regardless of how dic it might be to discuss mo tality or money, early pla ning can help aging entrepreneurs avoid selling t business—or selling ou children. *Kerry*

Tax tip: Give away shares, freezing the estate's value

POL DOLLS: *Johnson and Goldwater in 1964*

L THE RESIDENTS' EMORABILIA

Bob Dole, Steve bes, and the rest he GOP Presiden- contenders sharp- eir elbows along the pri- trail, another quadren- rite is about to up. The ar- of the pri- y season gs collec- of Presi- al buttons, rs, and oth- olitical para- alia out of hi- ation. These folks o scoop up everything can find, dreaming that 's items may prove to s valuable as artifacts the campaigns of Teddy evelt or John Kennedy. t not so fast: History- ed hobbyists warn es not to get blown by the political winds e moment. Before bet- the ranch on Lamar nder or Phil Gramm ns, you'd do well to con- the meager demand for Tsongas tchotchkes.

leed, winning counts it comes to the most ole political prizes, al- h there are notable ex- ns. Some collectors spe- in items from lential "hopefuls," promi- ools who failed to earn party's nomination, such uey Long or Nelson Rockefeller. Other history buffs concentrate on arcana from third-party candidates, such as early 20th century Socialist Eugene Debs, 1948 Dixiecrat Strom Thurmond, and Ross Perot. Still others crave materials from a politician's earlier career. Thus Ronald Reagan movie posters or "Harry Truman for Judge" items remain in vogue.

COLLECTIBLES

Sometimes a well-known candidate can rub off on an also-ran. In the Presidential election of 1920, Ohio Governor James Cox, a Democrat, lost to Republican opponent Warren Harding, who won in a landslide. Yet extremely scarce buttons depicting Cox and his running mate can be worth up to $50,000. How come? Cox happened to share the ticket with Franklin Roosevelt. Cox-FDR jugates, as buttons picturing two candidates are called, are among the hobby's most esteemed treasures. Other rare jugates worth $1,000 or more pair Harding with Calvin Coolidge (1920) and John Davis with Charles Bryan (1924).

FORGOTTEN FACES: *Parker and Davis ran in 1904*

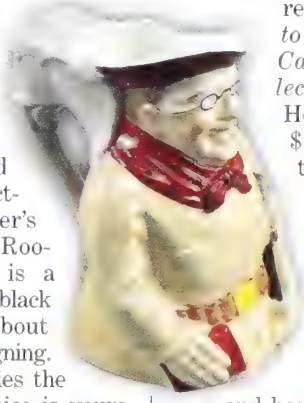
The most provocative pieces tend to reflect the history of a particular campaign. There are license plates with Herbert Hoover or Alfred Smith on them and china plates showing Grover Cleveland or William Taft. In his attempt to stymie a third term by FDR, Wendell Willkie unleashed a variety of slogan buttons including: "No Man is Good 3 Times" and "We Don't Want Eleanor Either." Some Willkie slogan buttons can be had for under $10.

NOT QUITE THE TICKET: *Dick and Pat in 1960*

"People don't have to like the candidate to collect the candidate," says David Frent, an Oakhurst (N.J.) collector and auctioneer (908 922-0768). "But they have to like the process and understand the history of the country." Washington (D.C.) collector Robert Fratkin cherishes a 1904 button issued by Democratic candidate Alton Parker in his race against Republican Teddy Roosevelt. A white bride and groom are depicted under Parker's picture; below Roosevelt's image is a white bride and black groom. Talk about negative campaigning. The button carries the slogan, "The choice is yours, it's up to you." Fratkin figures it's worth $6,000 to $10,000.

Experts suggest looking for "coattail" buttons in which a Presidential candidate is teamed with men and women running for local offices. Since these are typically produced in smaller quantities than the stuff from national campaign headquarters, they're often worth more. Along the same lines, look for items tagged to a single date or event.

Newcomers should consider joining the American Political Items Collectors organization (APIC). Membership costs $25 a year and includes a subscription to *The Keynoter* journal and a monthly newspaper, *Political Bandwagon*. Write to APIC at P.O. Box 340339, San Antonio, Tex., 78234. For a fine overview, read *Hake's Guide to Presidential Campaign Collectibles* (Wallace-Homestead Book, $17.95). The author, Ted Hake (717 848-1333), runs auctions and has published price guides on buttons.



BULLY: *Teddy Roosevelt's mug ended up on one*

WALKING CANES: *W. J. Bryan and William McKinley*

You'll have to wait to see whether the trinkets that you accumulate during the 1996 campaign will increase in value. And if, for example, Bob Dole wins the White House, demand for items from his try for the top job in 1980—or his Vice-Presidential run way back in 1976—should also pick up steam. If he loses, those who are heavy on Dole doodads can start thinking about the battle in 2000. In political collecting, as in politics, there's always the next time around. *Edward Baig*

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5 ❑ Finance, Insurance, Real Estate 6 ❑ Government 7 ❑ Transportation, Public Utilities
8 ❑ Service Industries 9 ❑ Other - Please Specify:

2 What is your title?

A ❑ Chairman of the Board B ❑ President C ❑ Vice President D ❑ Treasurer, Secretary
E ❑ General Manager F ❑ Division Manager G ❑ Department Manager H ❑ Other Manager
I ❑ Student J ❑ Other - Please Specify:

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ODUCTION AND LEADING INDEXES

hange from last week: –0.6%
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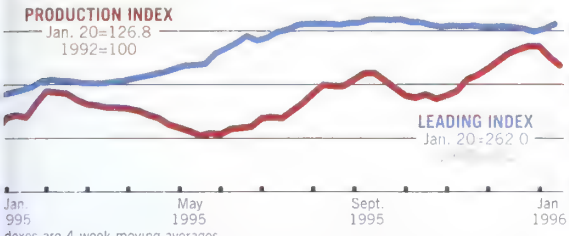

dexes are 4-week moving averages.

production index fell during the week ended Jan. 20. Seasonally adjusted ut of cars and trucks dropped, in response to high inventory levels. tric power output fell back after the previous week's blizzard pushed up gy demand. Before calculation of the four-week moving average, the index to 124.4, from 125.7.

leading index increased in the latest week, but the unaveraged index ed to 263.9, from 264.2, dragged down by falling materials prices.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (1/27) thous. of net tons	2,040	2,035#	2.1
AUTOS (1/27) units	106,552	107,267r#	–24.1
TRUCKS (1/27) units	113,710	98,705r#	–4.3
ELECTRIC POWER (1/27) millions of kilowatt-hrs	64,901	62,943#	3.1
CRUDE-OIL REFINING (1/27) thous. of bbl./day	13,697	13,772#	2.2
COAL (1/20) thous. of net tons	19,616#	17,149	–7.9
PAPERBOARD (1/20) thous. of tons	NA#	NA	NA
PAPER (1/20) thous. of tons	NA#	NA	NA
LUMBER (1/20) millions of ft.	449.7#	458.4	-6.2
RAIL FREIGHT (1/20) billions of ton-miles	23.6#	22.0	–1.7

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA[1], SFPA[2], Association of American Railroads

ADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
ICK PRICES (1/26) S&P 500	616.96	606.94	32.0
IPORATE BOND YIELD, Aaa (1/26)	6.81%	6.80%	–19.8
USTRIAL MATERIALS PRICES (1/26)	110.2	110.2	–4.7
INESS FAILURES (1/19)	NA	NA	NA
L ESTATE LOANS (1/17) billions	$507.3	$508.0	9.5
IEY SUPPLY, M2 (1/15) billions	$3,774.3	$3,757.2r	5.0
'IAL CLAIMS, UNEMPLOYMENT (1/13) thous.	316	394	–6.8

rces: Center for International Business Cycle Research (CIBCR), Standard & s, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures rge companies) Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on ness failures and real estate loans

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/31) $/troy oz.	405.550	402.500	7.5
STEEL SCRAP (1/30) #1 heavy, $/ton	144.50	144.50	1.7
COPPER (1/27) ¢/lb.	121.3	118.5	–16.9
ALUMINUM (1/27) ¢/lb	73.0	75.5	–29.8
COTTON (1/27) strict low middling 1-1/16 in., ¢/lb.	83.24	80.28	-6.8
OIL (1/30) $/bbl.	17.61	18.74	–4.6

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

TEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
ERAL FUNDS (1/30)	5.37%	5.44%	5.63%
IMERCIAL PAPER (1/30) 3-month	5.31	5.35	6.28
TIFICATES OF DEPOSIT (1/31) 3-month	5.24	5.36	6.22
ED MORTGAGE (1/26) 30-year	7.30	7.30	9.32
USTABLE MORTGAGE (1/26) one-year	5.45	5.59	6.83
ME (1/31)	8.25	8.50	8.57

ces: Federal Reserve, HSH Associates, Reuters Holdings PLC

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/31)	106.96	106.81	99.57
GERMAN MARK (1/31)	1.49	1.48	1.52
BRITISH POUND (1/31)	1.51	1.51	1.57
FRENCH FRANC (1/31)	5.11	5.08	5.27
ITALIAN LIRA (1/31)	1597.0	1591.5	1607.5
CANADIAN DOLLAR (1/31)	1.38	1.37	1.41
MEXICAN PESO (1/31)	7.375	7.450	5.450

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars.

' data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense ment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

CLE SALES

lay, Feb. 5 ▶ Sales of cars and light s likely fell sharply in January, to an al rate of about 14.5 million, after ing in December to a 16 million pace omestic and imported vehicles. Truck were especially strong, but auto mak- ad to offer discounts averaging a hefty 00 to close deals. So in January some ick was expected even before the bliz- and flooding prompted many con- rs to delay car purchases.

RNATIONAL TRADE

esday, Feb. 7, 8:30 a.m.EST ▶ The trade deficit for goods and services bly widened to $8.5 billion in Novem- ber, according to the median forecast of MMS International, one of The McGraw-Hill Companies. The deficit narrowed to $8 billion in October, but even the wider gap in November would indicate that foreign trade added to economic growth in the fourth quarter compared with the third. Exports and imports, which fell by about 1% each in October, likely increased in November. Higher oil prices, though, meant that imports rose at a slightly faster pace.

INSTALLMENT CREDIT

Wednesday, Feb. 7, 3 p.m.EST ▶ Consumer debt probably rose at an annual rate of 11% in December, faster than the 10.4% gain in November. Higher car sales likely lifted auto financing. The Federal Reserve has discontinued reporting the change in installment credit on a dollar basis.

UNEMPLOYMENT CLAIMS

Thursday, Feb. 8, 8:30 a.m.EST ▶ New filings for state unemployment benefits will probably drop to about 350,000 for the week ended Feb. 3. In the week of Jan. 20, claims soared to 413,000, but that was a bounce back after the blizzard along the East Coast closed many state offices and prevented out-of-work residents from filing claims. Still, on a four-week moving average, claims have been running about 370,000 for the past three months—a high level this far into an expansion.

This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

BusinessWeek ONLINE

Sunday

When small business goes in search of capital, it can be risky business. Read the Special Report in this issue on the increasing number of scams, then talk about how to avoid the scamsters with author Michael Schroeder of BW and watchdog G. Philip Rutledge of Pennsylvania.

Feb. 4

9 p.m. EST in the Globe

Downloads

Missed our recent conference on the future of troubled Apple? There were insightful comments from seasoned Apple watcher Tim Bajarin. Or how about the one on the best mutual funds for your investment goals, with BW's Jeff Laderman and Amy Arnott of Morningstar? You can download transcripts of all BW Online events in our area of AOL—now including our new twice-weekly chats about B-schools.

For a free trial diskette including 10 free hours on AOL, call 1-800-641-4848 and mention Business Week.

America Online

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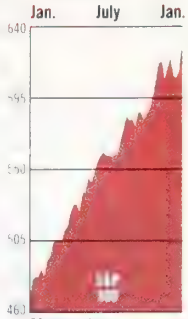
Postmaster

nvestment Figures of the Week

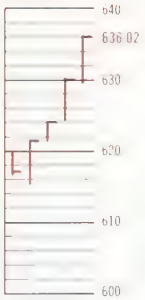
MENTARY

at week for Wall Street. First, -than-expected earnings re- whetted investors' appetites ocks. Then, the Federal Re- cut short-term interest rates uarter of a point, which is h for stocks as well. The Dow, g with a 5400 mark, was up for the week. Small and mid- ocks also jumped, but could ep up with the blue-chips. enough, in the face of a g economy, gold remained , with the spot price finish- e week at $406 an ounce.

STOCKS

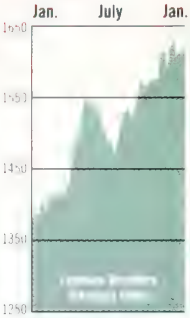


52-week change
+35.2%

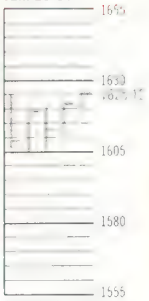


1-week change
+2.6%

BONDS

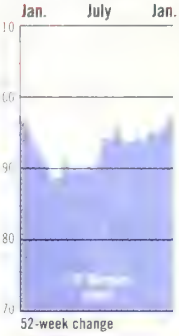


52-week change
+18.5%

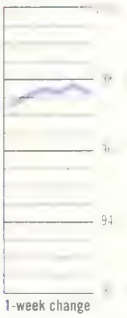


1-week change
+0.3%

THE DOLLAR



52-week change
+0.8%



1-week change
+0.3%

RKET ANALYSIS

TOCKS	Latest	% change Week	52-week
ONES INDUSTRIALS	5395.3	2.9	40.2
E COMPANIES (S&P MidCap Index)	220.8	1.8	28.6
COMPANIES (Russell 2000)	315.4	1.6	27.4
MPANIES (Russell 3000)	361.6	2.4	34.4

GN STOCKS	Latest	% change (local currency) Week	52-week
N (FINANCIAL TIMES 100)	3759.3	0.0	24.6
(NIKKEI INDEX)	20,812.7	2.5	11.1
TO (TSE COMPOSITE)	4968.4	6.1	23.6

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.04%	5.12%	6.05%
30-YEAR TREASURY BOND YIELD	6.02%	6.03%	7.74%
S&P 500 DIVIDEND YIELD	2.14%	2.22%	2.75%
S&P 500 PRICE/EARNINGS RATIO	18.1	17.3	16.1

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	571.0	568.0	Positive
Stocks above 200-day moving average	69.0%	66.0%r	Neutral
Speculative sentiment: Put/call ratio	0.60	0.56 r	Neutral
Insider sentiment: Vickers sell/buy ratio	1.57	1.50	Positive

BLOOMBERG FINANCIAL MARKETS

USTRY GROUPS

ONTH LEADERS	% change 1-month	12-month	Strongest stock in group	% change 1-month	12-month	Price
ENSE ELECTRONICS	25.4	146.8	LORAL	31.8	144.6	46⅝
D MINING	17.4	45.4	SANTA FE PACIFIC GOLD	27.8	47.6	15¼
S	16.1	55.8	HASBRO	41.9	48.5	44
ELS AND MOTELS	9.5	25.0	HILTON HOTELS	23.0	15.5	75¼
TAURANTS	8.7	45.5	McDONALD'S	11.4	53.4	50¼

ONTH LAGGARDS	% change 1-month	12-month	Weakest stock in group	% change 1-month	12-month	Price
CKING	–11.2	–15.6	CONSOLIDATED FREIGHTWAYS	–14.6	4.6	22¼
HINE TOOLS	–8.9	–0.9	CINCINNATI MILACRON	–9.5	2.2	23¼
NGS AND LOANS	–8.7	37.0	H.F. AHMANSON	–12.3	38.8	23¼
CE EQUIPMENT AND SUPPLIES	–8.4	24.2	ALCO STANDARD	–14.8	20.3	38⅞
ERAL MERCHANDISE CHAINS	–7.2	–1.0	KMART	–15.8	–56.4	6

TUAL FUNDS

RS

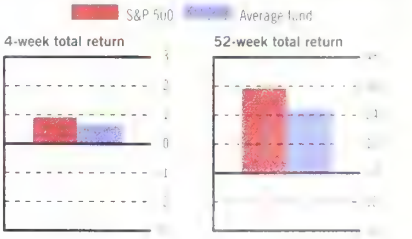
ek total return	%
ED SERVICES GOLD SHARES	23.2
GAN STANLEY INSTITUTIONAL GOLD	22.7
ICHARD PRECIOUS METALS	22.2

k total return	%
R CAPITAL APPRECIATION	83.3
S	83.2
LITY SELECT ELECTRONICS	77.3

LAGGARDS

Four-week total return	%
GOVETT SMALLER COMPANIES A	–9.9
RESERVE MID-CAP GROWTH	–9.3
KEYSTONE AMERICA HARTWELL EMERG. GR. B	–8.0

52-week total return	%
EV MARATHON GREATER INDIA	–31.8
AMERICAN HERITAGE	–24.7
STEADMAN AMERICAN INDUSTRY	–20.4



ATIVE PORTFOLIOS

mounts represent the value of $10,000 one year ago portfolio

tages indicate / total returns

U.S. stocks
$13,649
+2.83%

Treasury bonds
$13,100
+0.66%

Foreign stocks
$12,013
+0.43%

Money market fund
$10,564
+0.12%

Gold
$10,489
+0.72%

n this page are as of market close Wednesday, Jan. 31, 1996, unless otherwise in- ndustry groups include S&P 500 companies only; performance and share prices are as of market close Jan. 30. Mutual fund returns are as of Jan. 26. Relative portfolios are valued as of Jan. 30. A more detailed explanation of this page is available on request. r=revised

CAPITAL SPENDING: DON'T SKIMP NOW

Growth is fast becoming the mantra of Corporate America in the '90s, replacing the old standby of cost-cutting. Management consultants are burnishing their growth-strategy spiels, and smart CEOs are talking about growth as if it were the new frontier. With middle managers cut, bureaucratic layers flattened, and competencies shrunk to the core, the best "benchmark" companies are moving beyond downsizing to growing as the key to generating profits.

That's why the recent slowing in capital spending is so disquieting. For most of the current expansion, companies have been boosting investments at double-digit rates, aiming to improve efficiency and add capacity. The annual growth in manufacturing capacity, for example, has been running at 4%—twice what it was in 1992. This is one reason inflation hasn't been a problem, despite hand-wringing by the Federal Reserve, which has been overly restrictive.

The challenge now for CEOs is to keep investing for the long haul in the face of an economy that is weakening, thanks in part to budget bickering in Washington. Some are already cutting back investments, falling back into old patterns of tying capital spending to the business cycle. Others, with perhaps more foresight, are continuing to pour money into product innovation, improved efficiency, and new capacity, despite the current dip in growth from 2%-3% to 1%-2%. The long term is full of promise. The danger, of course, is that if too many fearful CEOs cut capital spending way back, an investment slump could throw the country into recession. This would be a tragedy.

ASIA: CLOSED MARKETS HURT GROWTH

Morgan Stanley & Co.'s growing success abroad attests to the effectiveness of open financial markets in generating growth. While the efficacy of open markets may appear obvious to Americans and Europeans, it is less so in Asia, where Japan has been championing a more closed model. It is now clear that this model is the major reason behind Japan's current banking crisis. The rest of Asia should take note.

Japanese officials from the Ministry of Finance and the Ministry of International Trade & Industry have been training Malaysians, Indonesians, Chinese, and others in Japan's own brand of banking. They argue that open financial markets led to the meltdown in Mexico, where, they say, hot money from abroad led to catastrophe. (Actually, the Mexican crisis was caused by secret government printing of pesos by the party in power before a key election.) Japanese officials say government-controlled banks are a better way to increase growth.

It turns out that the Japanese financial model is als surefire way to encourage corruption—and lower grov The current banking crisis is a made-in-Japan phenome caused by inept government officials in the MOF and ex-l bureaucrats at private banks working with gangsters v played the real estate game in the go-go '80s. The res Five years of stagnant economic growth for Japan.

Much the same thing has happened in South Korea, wh massive corruption involving the biggest corporations pay bribes to top government officials has roiled the coun Tight government control over bank financing, as well as crative contracts, led to a system of under-the-table p back by virtually all Korean companies.

Both cases show that a closed financial system based government-influenced banks can have terrible consequer Open markets mean open information; closed markets m connections and bribery as a way of economic life. Japa paying a high price for its financial model. The rest of doesn't have to follow. The open model offered by Amer financial institutions is far superior.

DO THE DEAL NOW

It's so depressing. After a year-long runup in expectat the budget isn't balanced, welfare isn't reformed, ent ment spending isn't curbed. For all the Sturm und Drar the Republican Revolution, there is nothing to show for is natural for politicians to want to walk away from whole process and wait until after the November electio start all over again. We hope they don't. There is still tim a deal—and we don't mean a measly "downpayment" th just political cover, but a real budget deal.

Truth is, the two sides are amazingly close in actual n bers. Yes, the Administration proposal saves most of real spending cuts for the last two years of the seven- plan. But the Republican program "backloads" most also. The differences over taxes and Medicare are s enough to split.

The real problem is posturing on principle. President ton is winning political points by pretending to save Medi but the only way to really do that is to curb the grow spending on this entitlement, as the GOP plan proposes. Republicans want to save the family with a huge tax c for children, but the real way to raise stagnant wag through fast economic growth. A balanced budget tha duces interest rates does that much better than a p designed tax cut that doesn't reward labor or investme

A bipartisan group of Blue Dog conservative Democra the House, centrists in the Senate, and House Republican trying to cobble together one final last-ditch plan for anced budget. Going home to run on a platform of fi pointing and accomplishing absolutely nothing in Washi can't be the best way to win in November for either p Do the deal now.

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FLAT TAX WHY IT'S SO RISKY

IESS WEEK
February 19

BusinessWeek

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THIS GUY IS HISTORY!

Angry consumers are forcing a revolution on the car lot

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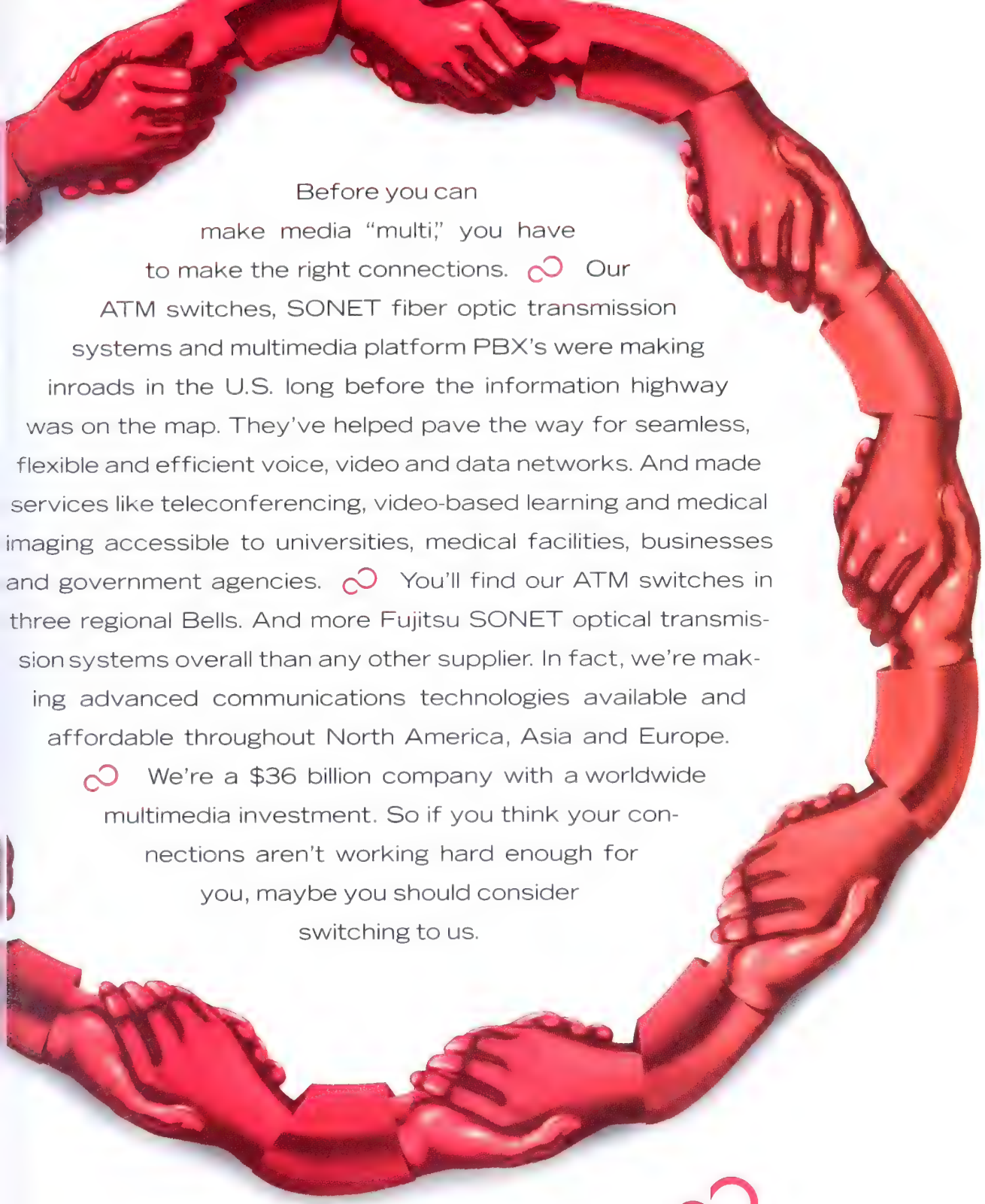

Before you can make media "multi," you have to make the right connections. Our ATM switches, SONET fiber optic transmission systems and multimedia platform PBX's were making inroads in the U.S. long before the information highway was on the map. They've helped pave the way for seamless, flexible and efficient voice, video and data networks. And made services like teleconferencing, video-based learning and medical imaging accessible to universities, medical facilities, businesses and government agencies. You'll find our ATM switches in three regional Bells. And more Fujitsu SONET optical transmission systems overall than any other supplier. In fact, we're making advanced communications technologies available and affordable throughout North America, Asia and Europe. We're a $36 billion company with a worldwide multimedia investment. So if you think your connections aren't working hard enough for you, maybe you should consider switching to us.

FUJITSU

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do is a lo

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make wise, productive decisions abo
money you're putting away for retireme
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well depend on it.

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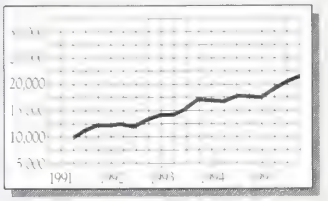
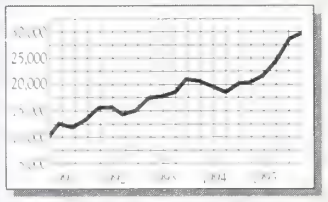
JANUS WORLDWIDE



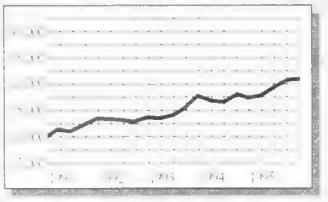
Value of investment: $21,589
Average annual returns (as of 12/31/95):
1 year + 21.90% 5 year N/A
Since inception (5/15/91) + 18.46%

WARBURG PINCUS EMERGING GROWTH



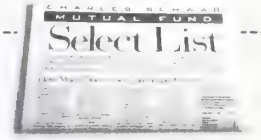
Value of investment: $29,813
Average annual returns (as of 12/31/95):
1 year + 46.27% 5 year + 24.42%
Since inception (1/21/88) + 18.39%

FOUNDERS WORLDWIDE GROWTH



Value of investment: $20,973
Average annual returns (as of 12/31/95):
1 year + 20.63% 5 year + 15.97%
Since inception (12/31/89) + 14.37%

MORNINGSTAR *Data provided by Morningstar, Inc. as of 12/31/95. These and over 350 funds are available through Schwab's Mutual Fund OneSource.*



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For an objective ranking of the historically high-performing funds available through Schwab, call for two free issues.

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Charles Schwab

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CAR HAPPY

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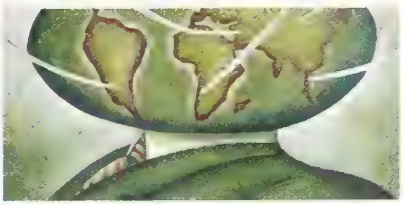

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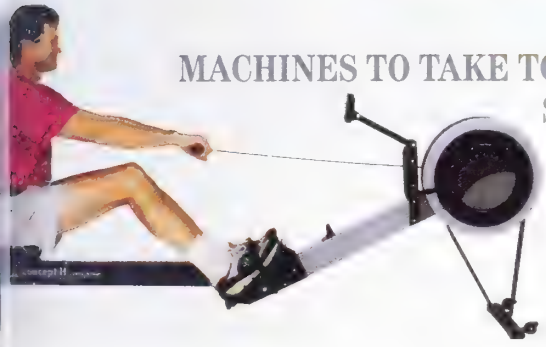

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Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

TALK SHOW "It's a fine piece of crystal. It won't take mu to break it"

—Nevada Governor Bob Miller, on the National Governors' Assn plans to revamp welfare and Medicaid, ending budget gridlock

IBM: *A winged ThinkPad*

MUSEUM PIECES

BUTTERFLY ON A PIN

IBM HAS TARGETED ITS NIFTY Butterfly laptop for extinction. On the market barely a year, the ThinkPad 701C notebook PC is a hit, but executives feel it will soon be outmoded.

The computer solves the problem of cramped notebook keyboards. Although its screen is only 8.25 inches wide, the keyboard spans 11.5 inches. How? The board is in two halves, which can slide into the 4.5-pound ThinkPad's tiny body. The computer has racked up 27 design awards and sold 215,000 units, making it the top-selling notebook PC of 1995, according to market researcher International Data.

Poor Butterfly. It's doomed because the next generation of IBM lightweight PCs will sport screens wide enough to allow a regular keyboard. Code-named Kite, the new ultrathin model (one inch thick and weighing about one pound) is due out later this year. No wonder Big Blue is discounting the Butterfly heavily of late. It started in the $3,900 to $5,600 range. But with the latest cuts, it's now $1,499 to $2,999.

The elusive-wing keyboard isn't dead yet. IBM insiders say the company's engineers are tinkering with the keyboard for use in a handheld device such as a personal digital assistant. *Ira Sager*

CAMPAIGN '96

NOW YOU CAN REALLY BUY A CANDIDATE

BOB DOLE'S STOCK HAS fallen—literally. The polls are one thing, but we're talking about Iowa Electronic Markets, a worldwide office pool where you can buy stock in a Presidential candidate.

As the crucial Feb. 12 Iowa caucuses approach, the hottest investment action surrounds the GOP race, which is fitting for a party that embraces market forces. Dole stock was 59¢ per share Feb. 7, down from its 62¢ peak four weeks before. Just as in the polls, publisher Steve Forbes is narrowing the front-running Kansas senator's lead, climbing from 10¢ to 18¢ during the same period. Dole, trading at 55¢ on Feb. 6, got a four-cent bump Feb. 7 after Senator Phil Gramm of Texas lost the Louisiana caucuses to commentator Pat Buchanan. In that one day, Gramm dropped from 12¢ to 5¢; Buchanan climbed from 5¢ to 7¢. If Dole wins the nomination, his current investors will almo double their money.

More than 5,900 peop have bet—er, invested—a tal of $41,500 in the 19 market, which the Univer ty of Iowa has run sin 1988. Regulated by the Co modity Futures Tradi Commission, the Iowa ball box bourse takes orde through the Internet (http www.biz.uiowa.edu/iem/) a pays off shareholde of the GOP winner ter the August R publican convention

There's also a p for the November ge eral election. Bill Cl ton (46¢) is wor slightly more than t unknown Republic contender (43¢).

Richard S. Dunha

DOLEFUL: *Bob's stock is down*

NEW WORLD ORDER

A SECOND TOUR OF DUTY IN NAM

THE WHITE HOUSE HAS A short list for the U.S. ambassadorship to Vietnam. And they're all veterans of the war that ended over two decades ago.

One prominent name is from the business world, that of James Kimsey, the founder of America Online. Kimsey has financially backed an orphanage in Vietnam for a number of years. Also on the list: Thomas Vallely, head of Vietnam studies at Harvard's Institute for International Development. He has Sen tor Bob Kerrey (D-Neb.) friend and fellow vet, pushi for him. Another candida is Representative Doug "Pete" Peterson (D-Fla.) former prisoner of war w isn't seeking reelection. Pl there's the No. 2 official at the Veterans Affairs Dept., Hershel Gober, an Arkansas native. He has traveled to Vietnam to assess Hanoi's cooperation in locating Americans missing in action. None commented about t list except Vallely, who s he had "heard" he was on

KIMSEY: *ambasso*

Although the U.S. a Vietnam normalized relatio last year, White Hou sources say a final decision still months away, awaiti the right political mome Reason: President Clinto avoidance of military servi makes Vietnam a touchy sue in an election year. Al some Republicans on the P aren't eager to accord Ha full relations. *Mark Lew*

THE LIST WHAT INFORMATION AGE?

The personal computer, on the scene for 15 years now, may be an indispensable tool for many, but hardly for everyone. A recent poll shows that for the average American, the PC ranks slightly below the hair dryer as an invention people can't live without. And that's despite all the hype about a wired world and strong computer sales. A possible reason: Those other inventions are easier to use.

DRYERS BEAT PCs

The car takes top honors: Some folks prefer cruising the highway to the I-way.

COULDN'T LIVE WITHOUT THIS INVENTION

INVENTION	PERCENT OF 1,005 SURVEY RESPONDENTS
AUTOMOBILE	63%
LIGHTBULB	54
TELEPHONE	42
TELEVISION	22
ASPIRIN	19
MICROWAVE OVEN	13
BLOW-DRYER	7.8
PERSONAL COMPUTER	7.6

DATA: LEMELSON-MIT PRIZE PROGRAM

EVERY YEAR THESE GUYS COME UP WITH 500 MORE REASONS FOR YOU TO HIRE US.

Yikes! They're busy passing over 500 legislative changes a year that can affect your business. But for the 250,000 employers (both large and small) who count on us, keeping up with this frantic pace is a breeze.

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Up Front

I-WAY PATROL

MORE HACKER-PROOF THAN THOU

WHO BEST GUARDS your sacred credit-card number for purchases over the Internet? One cybermerchant is charging that its competitors' security methods are easily breached. And that has touched off a counterbarrage of indignant "flame" mail from the rivals, who claim hackers can't outfox them.

STEIN: *Watchdog or fearmonger?*

First Virtual, the maverick electronic-commerce company headed by former celebrity manager Lee Stein, warns that evildoers might sneak inside your computer's software via game or screen saver programs offered free over the Internet. They would wait quietly for a card number to be typed in, capturing it before it is encrypted.

One solution, says First Virtual, is—ahem—to use its services. With First Virtual, you open an account by phoning in your card number. First Virtual gives you a password to use for Net purchases. Before clearing transactions, they E-mail customers to ensure legitimacy.

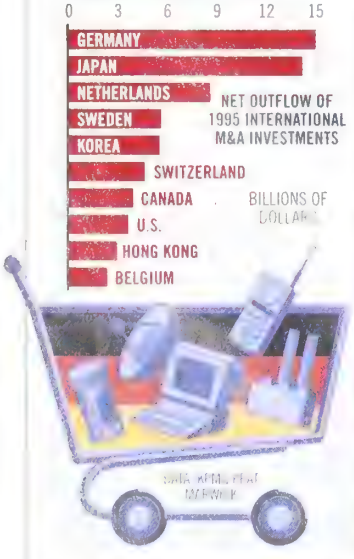
First Virtual's competitors are sputtering mad over its alarms. Its "sweeping claim is completely uncalled for," says Magdalena Yesil, a cofounder of rival CyberCash. Competitors say they have built-in safeguards to detect tampering. Plus, Visa and MasterCard say they are testing standard software to protect electronic transactions. *Kelley Holland*

DRAWN & QUARTERED

THE BIG PICTURE

FOREIGN FORTUNES

German investors went bargain shopping overseas last year. German outflows of money for mergers and acquisitions exceeded the inflow of such investments by $15 billion. The biggest buy: Hoechst's $7.1 billion acquisition of drugmaker Marion Merrell Dow.



BROADCAST NEWS

HOW NOT TO KISS UP TO THE NEW BOSS

WHEN ABC NEWS PLUGS THE network and its incoming owner, Walt Disney, the audience gets a warning. ABC's early-morning (2 to 5 a.m.) *World News Now* recently ran a spot on *The Mighty Ducks*, a Disney cartoon show scheduled to be shown next fall on the network. Under a picture of one of the hockey-playing mallards flashed the words "obsequiousness notification."

A spokesman for Disney, which is awaiting federal approval to acquire Capital Cities/ABC, was unaware of the jibe. "We have nothing to say about it," says Kenneth Green. Disney first brought out a 1992 movie on a peewee hockey team called *The Mighty Ducks* and in 1993 launched an Anaheim (Calif.) pro team by the same name.

The four-year-old ABC program's irreverent side has helped make it the top-rated overnight news show. And the oddly named hockey team team has long been a favorite target. When the show runs game footage of the Disney team, a duck call sounds in the background.

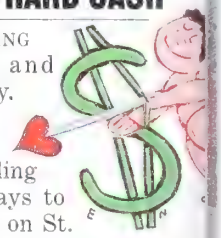
World News Now also has a history of tongue-in-cheek fawning over its superiors.

MIGHTY DUCK: *Dissing Disney*

Network honchos such as Chief Executive Thomas Murphy or news anchorman Peter Jennings are often shown in public appearances, with mockingly fulsome voice-overs (on Murphy: "He's the greatest boss") and that same flashing "obsequiousness notification." □

SALES TALES

WARM HEARTS, COLD HARD CASH



MARRYING cupid and cupidity, businesses are finding new ways to cash in on St. Valentine, or at least to promote themselves.

Take Carillon Importer which brings in Stolichnaya vodka from Russia. It invites Net surfers to send electronic Valentines, complete with hearts-and-flowers graphics, from its Web site (http:/www.stoli.com). Along the way, they'll likely get a Stoli sales pitch.

Then there's Manhattan's fabled Rainbow Room, which is throwing a V-Day wedding for the winners of an essay contest (topic: why the place is the ideal spot for nuptials). Two New York cops, Felix Rakowski and Stephen Gallagher, bested 950 entrants.

A recent poll by Primestar, the satellite-TV service, finds the most popular way to celebrate Valentine's Day is to go out to dinner (56%). Next is giving flowers (37%). Americans will send an estimated 925 million valentines this year at an average $2.25 each. Only Christmas is bigger for cards. Hallmark is bringing out a new line using thoughts from the book *Men Are From Mars, Women Are From Venus.*

FOOTNOTES Percentage of teens who think hanging out at the mall is "in": 64%. Percentage who think the Internet is "in": 70

Will your heart pound any less because it's safe?

Will your goose bumps care that it's practical?

Find your own road.

Will that giddy feeling deep in your stomach diminish because the 9000 is ranked the safest car in production?* Will your exhilaration be heightened by its turbo's outstanding fuel efficiency? Will the almost guilty pleasure of driving it be compromised by large interior and 56 cubic feet of cargo space? We don't think so. Experience turbo rush in the Saab 9000 CS.

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Readers Report

GRADING THE GOP FRESHMEN

Regarding "The House freshmen" (Cover Story, Jan. 29): To call these clowns "freshmen" is demeaning to millions of conscientious high school and college students. If the game isn't played their way, they will take their ball and go home. They label themselves as conservative, but just what is being conserved besides the fortunes of the rich? It is not conservative to allow our environment to be ravaged, our cities and schools to deteriorate, our infrastructure to collapse, our citizens to be slaughtered with assault weapons. Nor is it conservative to push through a $240 billion tax cut when they say they are for balancing the budget.

Instead of debating the merits of their proposed programs, they have resorted to terrorist tactics and blackmail—holding the government hostage and threatening default if they don't get everything they want.

Bruce Rollier
Ellicott City, Md.

In your article, you quote Jeffrey T. Grade, chairman of Harnischfeger Industries Inc., as saying that the freshmen are "inexperienced and unskilled, but maybe that's what we need." Does he pick his professional employees that way? Government demands skill and experience, not arrogance, fanaticism, insularity, intolerance, and a "feeding frenzy at the money trough," as you aptly call it.

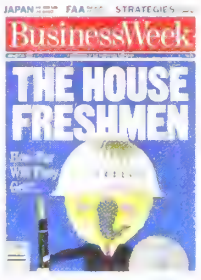
John E. Ullmann
Professor Emeritus of Management
Hofstra University
New York

The A- rating you gave the House freshmen on welfare reform is undeserved. The freshmen took a meat-ax approach to programs rather than considering the need to mandate work while addressing the issues of job creation, adequate and safe child care, and opportunities for skills development. T[he] long-term consequences of their p[ro]posed welfare reform will prove ve[ry] costly, both socially and economically.

Richard Rh[ee]
Tacoma, Wa[sh]

While I have noticed a more libe[ral] tilt in BUSINESS WEEK's articles over t[he] past two years, your comments rega[rd]ing the GOP freshman class in your ar[ti]cle "GOP rookies: Take 'yes' for an a[n]swer" (Editorials, Jan. 29) go beyo[nd] my threshold of tolerance.

While the GOP freshman class may [not] have been able to get the bulk of th[eir]



A POOR MARK

"Government demands skill and experience, not arrogance, fanaticism, insularity, intolerance, and a 'feeding frenzy at the money trough' "

agenda passed because of either a tie[d] Senate or President Clinton's veto p[ow]er they were responsible for bringing t[o] vote and passing in the House a majo[ri]ty of items in the Contract With Ame[ri]ca. This group of "young Turks," as th[ey] are routinely portrayed by the ma[in]stream media, represent the unclutter[ed] "get-the-job-done" view of many Ame[ri]cans. They should be congratulated [on] being the most potent political force [for] sound government change in 40 year[s].

K. F. Yo[ung]
Chairman, President, and C[EO]
Sybron Internatio[nal]
Milwauk[ee]

Your editorial was right out of [the] typical liberal textbook. If a few m[ore] people would get on the GOP freshm[an] bandwagon, then maybe we could get [to] where we want to go in this country [and] forward to prosperity.

James F[.]
Janesville, W[is.]

Business Week
A Division of The McGraw-Hill Companies

FEBRUARY 19, 1996 (ISSN 0007-7135)*** 3463

Single copies, $2. Write for rates in other countries.

Postmaster: Send address changes to BUSINESS WEEK, P.O. Box 430, at additional mailing offices. Postage paid at Montreal, P.Q. Canada Post

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Readers Report

CORRECTIONS & CLARIFICATIONS

The Mutual Fund Scoreboard (Feb. 6) reported some incorrect data for the Berwyn and Berwyn Income funds. For the Berwyn Fund, the correct yield is 0.1% and the in-state (Delaware) phone number is 302 324-4495. For the Berwyn Income Fund, the correct yield is 5.7%. The top portfolio holding is AK Steel Corp., comprising 2% of the fund's assets. The in-state phone number is 302 324-4452.

The liberal polling bias continues, even in BUSINESS WEEK! Your "Business Week/Harris Poll" asks this question: "A group of 74 newly elected House Republicans is insisting that President Clinton agree to their version of a balanced budget, and has been willing to shut down the federal government to force an agreement. Do you approve or disapprove of what the House Republicans are doing?"

Let me suggest a different question to "pulse" the electorate: "President Clinton is insisting that House Republicans agree to his own version of a 'balanced budget,' and has been willing to shut down the government to force an agreement. Do you approve or disapprove of what President Clinton, his Administration, and the House and Senate Democratic congressional members are doing?"

We expect this bias from the "mainstream" media, but not from a supposedly objective publication!

Walter Schild
Mesa, Ariz.

ENRON SHEDS LIGHT ON A POWER PROJECT

BUSINESS WEEK has failed to check facts before citing figures and reporting on Enron Corp. and its participation in the Dabhol power project in India. In your article "More power to India" (International Business, Jan. 22), it was reported that:

- Enron withdrew a suit seeking $500 million in damages from Maharashtra for the plant's cancellation;
- Enron lost a profit of $75 million from the sale of a 20% stake in the project to Entergy Corp;
- Enron has 29 global power and pipeline projects pending or under way in Bolivia, Brazil, China, and Turkey.

Although Dabhol Power Co. and the Maharashtra government are working very diligently to bring this project back online, DPC has not withdrawn arbitration pertaining to the project. Enron did not lose $75 million when the sale of an interest in the Dabhol project to Entergy did not proceed. While Enron has 29 global power and pipeline projects pending or under way, they are in nearly as many countries worldwide, not solely in Bolivia, Brazil, China, and Turkey.

L. Diane Bazelides
Vice-President for Public Relations
Enron Corp.
Houston

AIRBUS' SYSTEMS DIDN'T CAUSE CRASHES

In his review of *21st-Century Jet*, the story of the Boeing 777 (Books, Jan. 22), Michael J. Parks writes that the Airbus Industrie [electronic] "fly-by-wire" system was "implicated in at least two crashes." This comment is as defamatory as it is groundless. Official investigation into accidents of the A320 have clearly concluded that the aircraft, their systems, and engines were not to blame.

Robert Alizart
Vice-President for
Corporate Communications
Airbus Industrie
Toulouse, France

Editor's note: Reviewer Parks based his statement about Airbus' control system on information in Karl Sabbagh's book. An Indian government report on a 1990 Indian Airlines crash faulted "the failure of the pilots to realize the gravity of the situation." A French government report on a 1988 Air France crash found "no evidence of any mechanical or instrumental failure." Still, many French pilots dispute the notion that only pilot error was to blame for these incidents.

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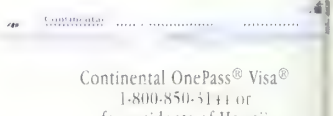

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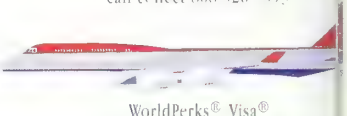

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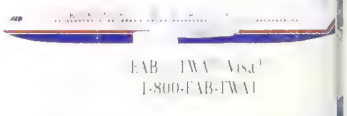

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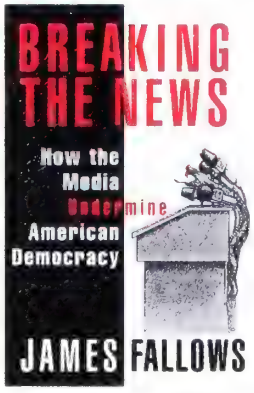
BREAKING THE NEWS
How the Media Undermine American Democracy
By James Fallows
Pantheon • 296pp • $23

HOT AIR
All Talk, All the Time
By Howard Kurtz
Times • 407pp • $25

ARE THE MEDIA GOING TO HELL IN A HANDBASKET?

Media, oh media, how do we hate thee? Let us count the ways. Americans today distrust not just their government but the sources of news about their government. From strangers to our own family members, folks tell those of us in the business about it constantly. "You media people," goes the refrain, "are a bunch of arrogant, untrustworthy windbags who slant the truth and only stir up trouble."



Now come two journalists' books purporting to document what the public suspects: America's media are indeed going to hell in a handbasket. In today's America, "the media actually get in the way of efforts to deal with important issues," James Fallows asserts in *Breaking the News*. The media sabotage crucial initiatives such as health-care reform and scare people away from public service by focusing on scandals and spectacle and away from critical issues. *Washington Post* media writer Howard Kurtz aims at a much easier target in *Hot Air:* America's new "talkathon culture." He surveys a wide assortment of pundits, commentators, and hucksters, including some who pose in journalistic garb to dress up their sensationalism. The price? "The national conversation has been coarsened, cheapened, reduced to name-calling and finger-pointing and bumper-sticker sloganeering," he asserts.

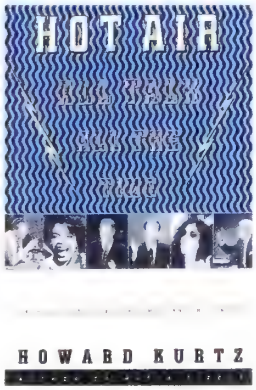
You'll find no knee-jerk defense of my craft here. Both books are delicious to read, puncturing the pompousness, fatuousness, and ethical backsliding that have indeed crept into America's media. But the books are also interesting because the authors—posturing as media high priests—are conflicted about what precisely the problem is. And in the end, both miss the bigger picture: Our industry is in the throes of a revolution that should correct most abuses.

Fallows hits on two key problems. In political coverage, "the reportorial elite" are constantly handicapping popularity races rather than concentrating on issues of substance. Then there's the journalistic "gravy train." Instead of lusting to uncover another Watergate scandal, reporters try to get on TV so they can later command lucrative speaking fees. "The best-known and best-paid people in journalism now set an example that erodes the quality of the news we receive and threatens journalism's claim on public respect," Fallows argues.

For example, both he and Kurtz tell how Tim Russert, moderator of TV's venerated *Meet the Press*, recently took his act onto the stage of an American Banker's Assn. convention in New York, posing tough questions for Senate Majority Leader Bob Dole (R-Kan.) and Treasury Secretary Robert E. Rubin to entertain the elite money crowd. Dole and Rubin are barred by federal ethics laws from accepting speaking fees. But Russert walked off with $20,000, according to the ABA. It's one thing to get paid big bucks by the network you work for, it's another to use your visibility to collect from people you may have to report on. Yet Russert didn't see how this might be perceived as ethically questionable.

This problem is easy to fix. BUSINESS WEEK and many other media outlets bar such payments to their journalists, and the TV networks have recently begun curbing honoraria. Amen.

If Fallows' work is something of a meditation, Kurtz's is a livelier, more journalistic investigation. He takes the reader backstage with the likes of Larry King, Howard Stern, and Phil Donahue, who make candid confessions about the failings of their occupation. When a college student asks Ted Koppel what advice he would give young people considering a career in journalism, Kopp answers dryly: "Get a good make man." How depressing.



Both books are at their best wh they skewer what Kurtz calls the "dri by journalism" of such commentators George Will, former *U.S. News & Wo Report* editor David Gergen, and A News commentator Cokie Roberts. E as Fallows and Kurtz wade into the w and crazy world of talk radio, dueling pundits, and instant-audience-reacti shows, they lose their focus. Fallow for example, condemns talk radio keeping alive rumors— driven by par san critics of the Clintons—that Wh House lawyer Vincent Foster was t victim of a Whitewater murder plot, a suicide. But he fails to see the ex tence of a corrective mechanism: In tir the Foster rumors were silenced by t media's own follow-up investigations.

Kurtz is similarly conflicted. He ske ers talk radio. But at the end of l book, Kurtz tells us that he hosted own Washington radio talk show, wh was canceled as a result of poor r ings. He attacks those who accept h oraria, then reveals (to his credit) th he has taken some himself but now cepts only those from more benign n profit groups and universities. He sails the intoxicating appeal of televis appearances, yet his is a common f on talk shows, where he happily opir on the sins of the media.

Both authors overstate their ca missing the fact that our industry bursting at the seams in a dynamic p riod of growth and change. From line news to wire sources to ever-e panding cable channels proliferating niche mag zines, America is drowni in information. For eve Rush Limbaugh, there is SPAN's unfiltered broadc of congressional committ hearings. For every ra shock jock like Stern, ther CNN host Larry King, givi viewers a kinder, gent view of guests. The me industry is far from perfe but it's moving in the rig direction—providing m diverse and unfettered coverage events so that people can make up th own minds. It's up to consumers choose their information wisely and r rely on journalists or the government choose for them. That's what Americ democracy is about.

BY DOUGLAS HARBRECHT

Harbrecht is BUSINESS WEEK's Wa ington news editor.

STEPHEN H. WILDSTROM

PPLE'S QUIRKY 'OWERHOUSE

e new PowerBooks me with a lot of mph–and some rious omissions

The history of portable computing for Macintosh users has been alst as quirky as the history Apple Computer itself. ien the first portable DOS chines appeared in the l-1980s, Mac users had to tch from the sidelines. ien Apple finally released laptop PowerBooks in '1, they were technologily more advanced than 'thing else on the rket. But in re- t years, Ap- allowed its tables to behind the el-based pack. Good news has been ghty scarce for Apple fans tching the company's tra- ls, but the newest genera- n of PowerBooks is at st a step in the right ection. Built with the werPC processor, they of- power equivalent to Pen- m-based Windows laptops competitive prices. But werBooks display the ne mixture of brilliant iches and serious omis- ns that often make Apple ducts simultaneously fas- ating and frustrating.

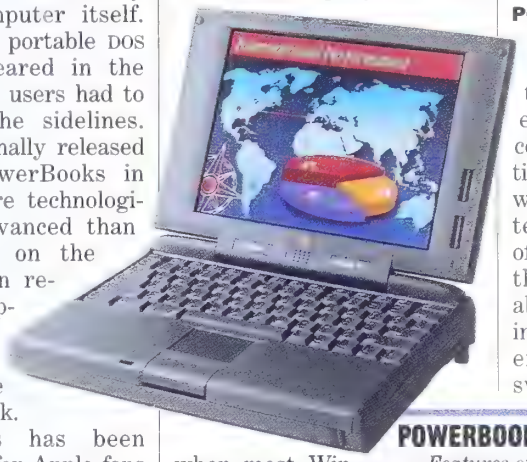
I wrote this column on the -of-the-line model, the 000 PowerBook 5300ce, h a 117-megahertz proces- ; 32 megabytes of random- ess memory, and 1.1-giga- e hard drive. Other 5300 dels line start as low as 799 for a unit with a 100- z processor, 8 MB of RAM, and a monochrome display.

Like all Apple products, it is graced with a handsome and well-thought-out design that makes it a pleasure to use. But this is far from a perfect notebook. Although the display is bright and crisp, the 10.4-inch screen seems a little puny at a time when most Windows machines in this class sport 11.3-inch or even 12.1-inch displays. The tendency of early production units to burst into flames while recharging forced Apple to switch from a lithium-ion battery to less-advanced nickel metal hydride, which limits battery life to a skimpy 2½ hours or so. The hard drive is not removable, and there's no provision for desktop docking. The only Mac to offer docking is the ultralight PowerBook 2300c/100 Duo.

The most grievous shortcoming, however, is the lack of a CD-ROM drive. Although the floppy drive can be removed, the bay isn't big enough for a CD-ROM, which is now an option even on many midpriced Windows laptops. It's easy to connect an external CD-ROM drive to the PowerBook, but the resulting setup isn't very portable. Since the most loyal Mac users are designers, multimedia programmers, and other creative types for whom the CD-ROM is an essential tool, this omission is nothing short of weird. Apple is planning a CD version eventually, but it will require an expensive redesign of the case—and probably more battery power.

PC CARDS. Although the PowerBooks trail Pentium laptops in some respects, there's still a lot the designers of Windows notebooks could learn from Apple. The tight integration of hardware with the Mac operating-system software avoids many of the compatibility problems that plague Pentium portables even under the much-improved Windows 95. For example, I was able to switch among PC card modems from Global Village, Megahertz, and TDK without installing any software. And the Global Village combination modem/Ethernet card gave me direct access to the office network simply by plugging it in and telling the PowerBook what sort of network I was using; I didn't even have to reboot.

For Mac users, the latest PowerBooks offer a welcome burst of computing punch on the road. But their elementary shortcomings illustrate one reason Apple has landed in so much hot water: a tendency to get things almost, but not quite, right.



POWERBOOK LINE

Features of the PowerBook 5300s (5300ce shown)

PowerPC 603, 100-117 MHz

500 MB-1.1 GB

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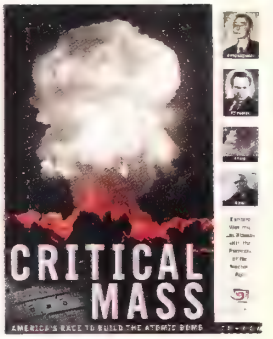
BULLETIN BOARD

CD-ROMS

BUILDING THE A-BOMB

Corbis Corp., the Bill Gates company that recently acquired the Bettmann Archive of historic photos and drawings, shows off its flair for history in *Critical Mass: America's Race to Build the Atomic Bomb.* The $50 Windows CD-ROM (a Mac version is due in March) illustrates the work of the Manhattan Project with a wealth of photographs from the archives of the Los Alamos National Laboratory. Video is sparingly but effectively used, including a ghastly animation in which Bert the Turtle teaches 1950s Americans how to duck and cover.



THE WEB

TAX FORMS ONLINE

Finding an obscure federal tax form no longer means a trip to the library or an Internal Revenue Service office. All IRS forms are now available through the World Wide Web, although retrieving what you need is a lot harder than it ought to be. Pointing your Web browser to http://www.ustreas.gov:803/treasury/bureaus/irs/c.taxforms.html will let you search for a document by keyword or form number. To read or print it, you'll need a free copy of Adobe Acrobat Reader. I suggest downloading the program directly from http://www.adobe.com.

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BY RUDI DORNBUSCH

BACK TO THE GOLD STANDARD? ONLY IN STEVE FORBES'S DREAMS

OFFBEAT: With inflation under control and currencies fairly stable, the proposal is unrealistic at best–and risks deflation at worst

Would-be President Steve Forbes has spent himself to the top of the Republican contenders. His bold promotion of the flat tax, the next best thing to no tax, has excited the interest of all those fed up with Washington politics, big government, oppressive taxation, winter snow, and middle age. Yes, it would be nice to have low taxes. But the flat-tax proposal can go nowhere. Cleansed of sacrosanct exemptions such as home-mortgage interest, the tax rate required in a flat tax is too high for the middle class. End of story. In the meantime, until people figure it out, the flat-tax idea will keep Forbes going in New Hampshire and beyond.

If the flat tax has a certain economic appeal, the same cannot be said of Forbes's second leg—the return to a gold standard. True, President Reagan established his right-wing credentials by dangling the return-to-gold prospect before his constituency. Whether gold was the right answer or not, at the time—in the late '70s and early '80s—the idea was worth weighing. Inflation was high, the dollar was unstable, and there was a serious need to bring back sound money. After his election, the President appointed a commission to study a return to gold, and there were hearings. Some gold nuts had their 15 minutes of fame before Congress, and the whole affair was quietly buried.

NO SUPPORT. Now, with inflation low after falling for more than five years, currencies relatively stable, the dollar rising, and unemployment below 6%, there is again talk of a gold standard. But who but a gold bug would think of bringing gold into the discussion of current policy, when deflation appears as much of a threat as inflation?

U.S. monetary policy has had its critics. Back in the '70s, Milton Friedman tirelessly knocked the Fed for its constant fine-tuning, which more often than not generated inflation rather than long-term growth. The Fed was more worried about recession than inflation, and its policies tended to err on the side of expanding money. But Friedman was the first to debunk Reagan's gold proposal. I am not aware of any single conservative monetarist economist coming out in support of gold.

There are many schemes around that purport to "fix" the Fed. There are rules for monetary aggregates, targets for stable price levels, and whatnot. Today, moving to a gold standard seems to any and all a completely offbe idea that offers more problems than solutio

The case for gold always has rested two arguments: Gold, because of its limit supply (unlike paper money that can be pri ed day and night) commands a stable pu chasing power over time. Hooking the m tion's money to gold takes away the discreti of central bankers to print money—and su stitutes in its place a naturally stable anch

POLITICAL FORCES. But several facts sta in the way of the gold myth. First, gold do not have a stellar record in terms of stabili South African, Russian, Asian, and Midd Eastern politics play a significant role in t price of gold. One reason gold is up to $4 an ounce is China's recent threat to inva Taiwan. Second, tying the U.S. to gold wou not stabilize currencies unless our chief tra ing partners did the same. Germany isn't i terested. It doesn't have an inflation pro lem, just as we do not.

Forbes argues that a move to gold wou instantly lower interest rates by up to 200 b sis points because the prospect of inflati vanishes. But what about deflation, a curse the world economy when it was on the go standard in the 19th century and during t Great Depression? Over the past decade, t U.S. has shifted from a high-inflation to low-inflation environment. Interest rates a starting to reflect that fact, though there some room to go.

It would be a costly exercise, with unce tain payoff, to experiment by entering a go standard, simply because of promises of ev less inflation. If we as a nation want to sho for zero inflation, we can try passing a bill i structing the Fed to focus only on price st bility, rather than employment as well as inflation. Set a reasonable framework for t transition so that growth isn't harmed. A create rules on how to deal with exceptio disturbances. Before Congress is a bill fro Senator Connie Mack (R-Fla.) that does ju that.

Forbes is a new kind of populist. He promi es heaven on earth—low taxes and stable mo ey—while trying to sweep away governme the Federal Reserve, common sense, and co promise. He wants a hookup with gold in t age of the Internet. In the end, none of th will happen, fortunately, and the U.S. will co tinue to enjoy low inflation, high employme and steady growth.

Rudi Dornbusch is professor of economics and management at Massachusetts Institute of Technology

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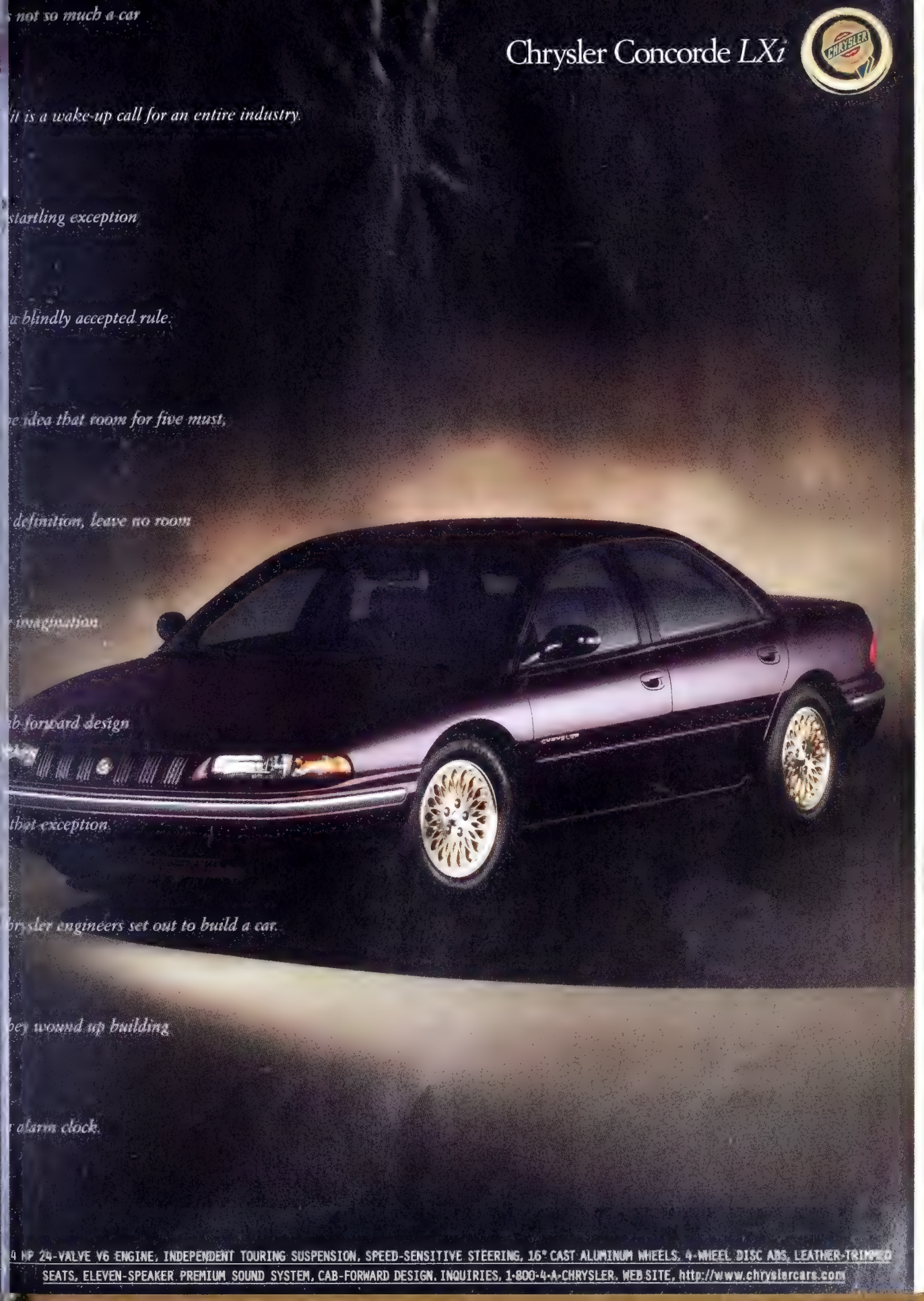

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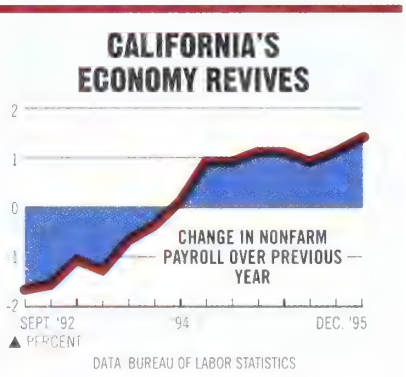
BY MICHAEL J. MANDEL

IT'S THE GOLDEN STATE AGAIN

Tech leads a resurging economy

During the first half of the 1990s, the state of California seemed to be laboring under a curse. Floods, fires, riots, government financial problems, and massive cutbacks in defense spending all conspired to keep the state's economy in low gear. As late as 1993, California's job rolls were still shrinking. Indeed, the troubles in California—which accounts for 11% of U.S. employment—may have significantly held back overall U.S. economic growth.

Yet a newly resurgent California may help keep the weakening U.S. economy afloat this year. According to a recent report from David Hensley and Kathryn Chin of Salomon Brothers Inc., job growth in California in 1996 could reach 3%, far greater than the projected national average of 1.4%.



One key reason for the positive outlook, they note, is that "California's aerospace bust is drawing to a close." For example, after losing 85,000 jobs in 1993 and 1994, aerospace losses slowed to a much more manageable 16,000 in 1995. Instead, California is riding the technology and entertainment boom. Business services—which include computer software—have generated 90,000 jobs over the past year, while the movie industry added another 15,000.

The economic surge in East Asia is reviving California's manufacturing sector. A study from Regional Financial Associates Inc., an economic consulting firm in West Chester, Pa., observes that merchandise exports make up 9% of California's economy, up from 5% in 1985. By comparison, defense spending now is only 4% of the state's economy.

California still suffers from a reputation as an expensive place to live and work. But that, too, is changing. In 1995, prices rose by a minuscule 1.0% in the Los Angeles area, and only 1.9% around San Francisco, far less than the national average of 2.6%. As a result, the state may be able to reduce the outflow of businesses and workers that has plagued it in recent years.

A BREAK FOR THE POOR

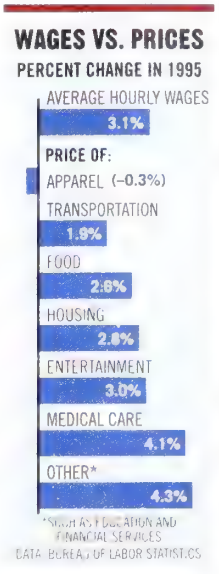
Lower inflation helps them most

In 1995, workers saw their hourly wages rise an average of 3.1%, slightly lower than the 3.2% annual increase in the second half of the 1980s. But their dollars are going further—inflation last year was only 2.6%, compared with a 4% rate in the earlier period.

The gains from lower inflation, though, are not evenly distributed. Price increases have slowed the most for necessities such as food and medical care, rather than luxuries such as entertainment. That may mean that low-wage workers—who spend more of their income on necessities—are doing better than the overall numbers indicate.

Food prices, for example, registered a 2.6% increase in 1995, down substantially from their 4.6% annual increase in the second half of the 1980s. That's a big plus for lower-income households, which spend about 17% of their money on food, compared with food's 12% share in upper-income budgets. And the substantial slowdown in health-care inflation may also be helping poorer workers, who devote more of their resources to health care—in part because they are less likely to have health insurance.

What about housing? In the 1980s, lower-income households, which put about one-third of their spending into shelter, saw their wages lag behind housing cost increases. Now, their earnings are rising somewhat faster than housing inflation.



REMEMBER M2? IT'S BACK

And it's raising red flags

Over the past few years, many economists—including Federal Reserve Chairman Alan Greenspan—have voiced increasing skepticism about using movements in the money supply to forecast economic growth. The once reliable M2 measure of money—which includes checking and savings accounts—stagnated between 1992 and 1994, despite the economy's recovery, as more people moved their savings into bond funds.

Now, a new study from the Federal Reserve Bank of Cleveland suggests that M2 may be regaining its potency as a forecasting tool. Economists John J. Carlson and Benjamin D. Keen find evidence of a permanent shift in the link between M2 and the real economy from 1990 to 1992, allowing faster economic growth without commensurate increases in the money supply. But now, they say, "the relationship between M2, inflation and output may have stabilized."

If they are right, then M2 is flashing warning signs. Toward the end of 1995, money growth slowed sharply, to an annual pace of only 2.6%. At that rate, the economy is due for a further slowdown in the second half of 1996.

ABUNDANCE CAN BE A CURSE

Resource-poor nations do better

It's only natural to envy countries with abundant natural resources. Being able to fund economic development with sales of oil or minerals would seem an advantage in the economic race.

But a new study from Jeffrey D. Sachs and Andrew M. Warner of the Harvard Institute for International Development confirms what was already suspected: Natural wealth is more likely to be a hindrance than a help for developing countries. Economic data over two decades show that "resource-poor economies often vastly outperform resource-rich economies," say the economists. Many oil-producing economies, for example, have not used their wealth to build up an industrial base, leading to slow growth in the 1980s. Sachs and Warner suggest that a strong mining or agricultural sector draws resources away from manufacturing, which has much more potential for long-run growth.

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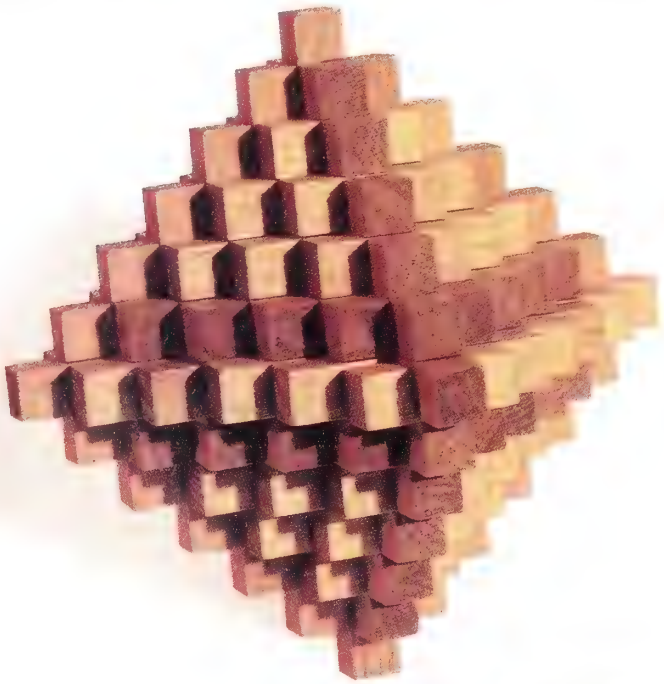

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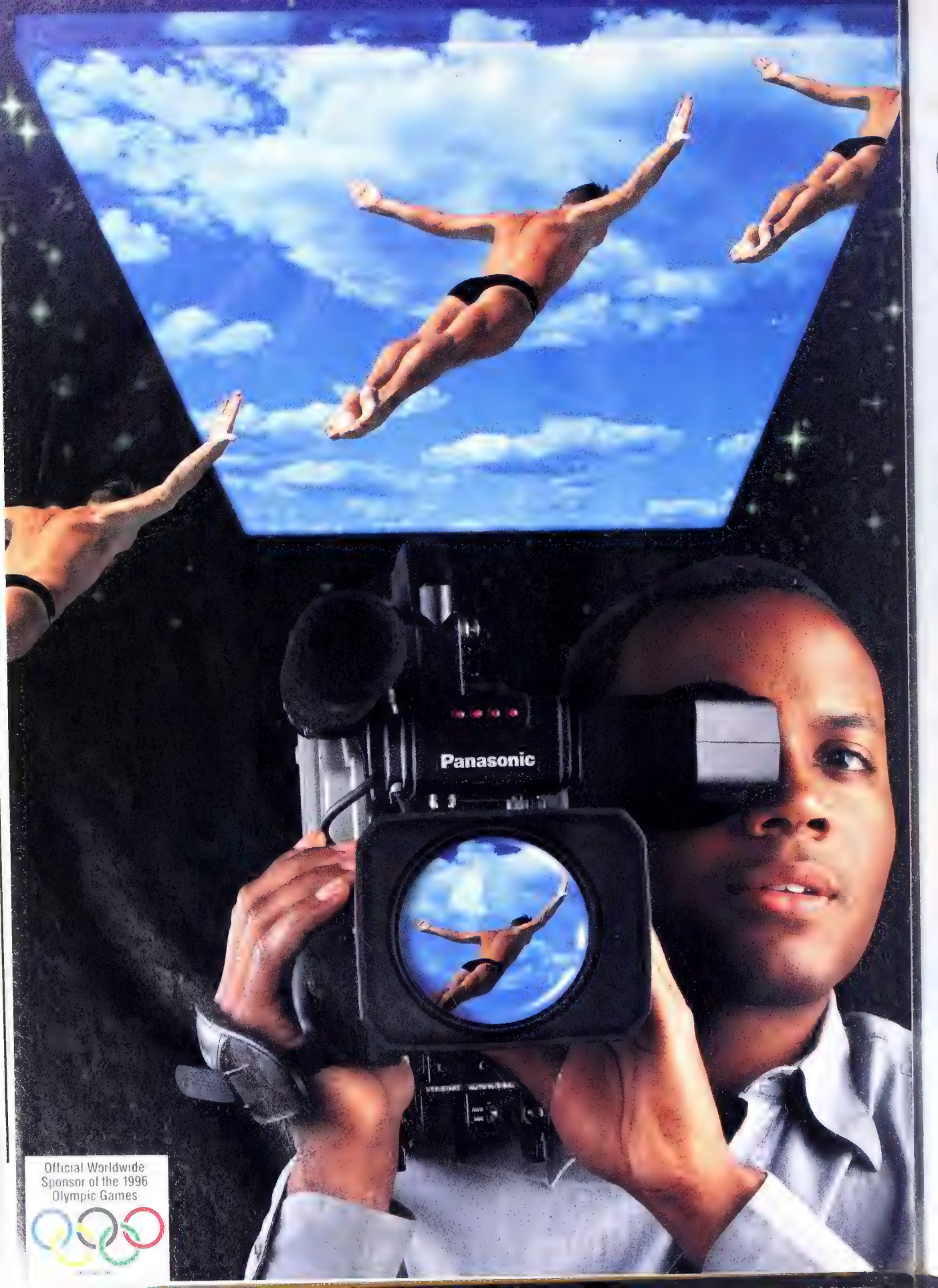
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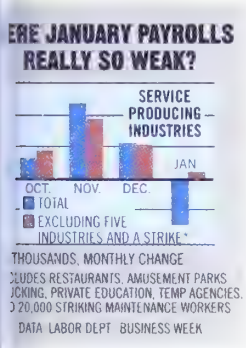
JAMES C. COOPER & KATHLEEN MADIGAN

BUNDLE UP AND WAIT FOR THE THAW

U.S. ECONOMY The recent grim economic reports show a sea change from ew weeks ago. True, at the end of 1995, the economy s taking on a softer feel. But suddenly, the data ve all the firmness of Jell-O, and recession worries are pping up. All this is bound to complicate Federal Reve policy, and it threatens to elevate the economy to ey election issue.

On the surface, the January reports clearly look resionary. Payrolls plunged, joblessness rose, purchas- managers sounded glum, and consumer confidence se-dived (charts). Amid higher commodity prices, en the inflation news is not all good.

But below the tarnished patina, the numbers were ewed by January's winter storms and the second vernment shutdown. In particular, the Labor Dept. k its employment survey during the week of the blizd. And given the record cold that gripped much of nation in early February, the numbers may not ow much bounceback until March.



The weak data can't all be blamed on the weather, though. Consumers have increasing debt to pay off, and the manufacturing sector is genuinely soft. Many factories are cutting back because of excessive inventories—particularly in the auto industry.

On balance, the economy's growth rate seems likely to have slipped from the third rter's healthy 3.2% annual pace to less than 2% in fourth quarter. Moreover, since 1995 ended with a imper and the weather and the shutdown started the t quarter at such a low level, the winter economy ld be hard-pressed to show any growth at all.

OKING TOWARD THE SPRING, though, there is hing to suggest that the economy cannot resume wing at least moderately. Prior to January, the labor rkets were generating income gains sufficient to pport trendlike growth in consumer spending. rough early February, the pattern of initial jobless ms points to continued modest growth in payrolls. An improving trade deficit, fueled by a sharp slowvn in imports relative to exports, will also support wth. The trade deficit for goods and services fell to 1 billion in November, from $8.2 billion in October. provement in the trade gap, by itself, is on track to add about a percentage point to fourth-quarter growth in real gross domestic product.

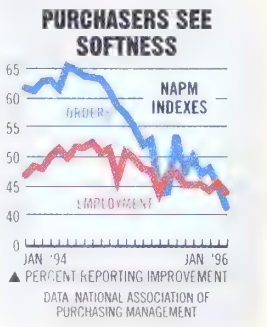
Moreover, capital spending is slowing down, but it will continue to grow much faster than the overall economy. The inventory adjustment begun last year is probably about over. And the Fed has started to ease monetary policy by cutting short-term interest rates.

In short, there are none of the classic imbalances that could set in motion the recession process, in which falling economic activity begins to feed on itself, causing the economy to spiral hopelessly downward.

What remains key to the growth—as opposed to recession—scenario is lower long-term interest rates. Rates will have to remain at 6% or below to assure support for housing and other important credit-sensitive sectors. But spooked by the budget fiasco, and most recently by a record Treasury refunding and inflation worries from gold and commodity prices, the bond market has kept the yield on the 30-year Treasury above 6.1%, even after news that payrolls tumbled in January.

THE WEATHER'S IMPACT on jobs last month was as obvious as a six-foot snow drift. Payrolls dove by 201,000 employees, the largest drop since the 1990-91 recession. Jobs had grown by 212,000 in November and 166,000 in December. Payrolls of service producers, which had grown by an average of 147,000 per month in the second half of 1995, dropped by 141,000 in January. And the workweek fell 36 minutes, to 33.7 hours, the largest decline on record.

The losses in jobs and hours worked were a quantum leap from those predicted by back-of-the-envelope models based on known data such as initial claims, the purchasing managers' employment index, and the Conference Board's help-wanted advertising index.



Moreover, a strike of building maintenance workers in New York, plus five weather-sensitive industries, accounted for 82% of the January job losses. Those industries—restaurants, amusement parks, private education, trucking and warehousing, and temporary-help agencies—make up only 12% of the total nonfarm jobs in the Labor Dept.'s survey of 349 industries.

Other distortions embedded in the numbers are harder to dig out. At least some of the 72,000 drop in man-

ufacturing payrolls also reflected the weather, as well as government contract work lost by many private-sector companies. The factory workweek shrank by nearly 1½ hours, to 39.8. That was one of the three largest monthly declines in the postwar era.

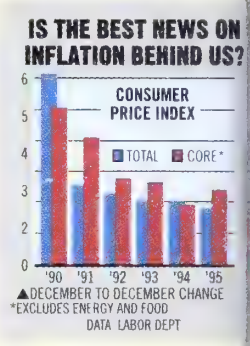
HOWEVER, NOT ALL OF THE SOFTNESS in manufacturing can be blamed on snow. The National Association of Purchasing Management's composite index of industrial activity weakened further in January, to 44.2% from 46% in December. The index has been below the 50% mark—the dividing line between growth and decline in the factory sector—for six months in a row, and last month's reading was the lowest in nearly five years. Weather and the shutdown may have played a part in the drop in production and jobs, but the plunge in January orders seems less likely to be distorted.

One problem: Auto makers are wrestling with inventories which had swelled to an 83-day supply at the start of the month; 60 days is normal. In January, total vehicle sales fell to an annual rate of about 14 million, after an incentive-fueled surge to 16 million in December.

Although that two-month average is respectable, auto makers have to hold their output below sales so they can trim inventories. That process will be a drag on first-quarter industrial production and economic growth. Looking toward spring, however, fewer vehicl on car dealers' lots will allow output to resume growi

But if the economy avoids a recession in 1996, do that mean inflation has nowhere to go but up? T runup in materials prices and gold prices rising abo $400 an ounce suggest that market-scaring idea.

Commodity prices, measured by the Knight-Ridder/Commodity Research Bureau's futures index, hit a seven-year high recently. Also, the Labor Dept.'s final look at 1995 inflation shows that the core consumer price index, which is a better indicator of inflation's underlying trend, accelerated slightly last year for the first time in five years (chart).



If anything, the blizzard ensured that the economy is growing below its noninflationary trend of about 2%, u ing the new GDP measure. That precludes any large lasting pickup in inflation. In fact, much of the rece rise in commodities reflects surges in the prices grains and gold. Industrial materials are softening.

The upcoming news on the economy is bound to bad. But consider this the groundhog phase of t slowdown. In six weeks, the economy's outlook w look much warmer.

GERMANY

RECESSION FEARS WON'T FADE AWAY

German industry posted some good news in December, but the economy remains on a recession watch.

Industrial production rose 0.6% in December, even though analysts had expected a decline of similar magnitude. Manufacturing output was up 2.1%. Still, output in the fourth quarter was down at a 4% annual rate from the third, a sign that Germany's real gross domestic product probably fell last quarter after no change in the third period. However, December's gain followed a 0.9% rise in November and was fairly broad—only construction output fell. Those factors suggest that the worst of the production losses may be over (chart).

A real upturn may take some time. Manufacturers must cut an inventory overload, caused by less foreign demand. Exports were hurt by the strong mark, high German wage costs, a softer U.S. economy, and, in the fourth quarter, the strike in France. The mark's weakening since last spring has helped the outlook, but exporters' prospects will depend on an easier monetary policy.

At least domestic demand is holding up. True, the jobless rate hovers near 10%, but the 1995 wage pacts were mostly generous for those with jobs, and a January income tax cut will lift disposable income. As a result, retailers' business expectations have improved.

On Jan. 30, the government of Chancellor Helmut Kohl announced a "50-point" package set on halving unemployment by 2000. Although the plan won't do much for 1996 growth, the government hopes to encourage business start ups and cut local business taxes.

While Bonn is trying to spur growth, the Bundesbank is moving less aggressively. The Buba trimmed its repurchase rate from 3.4% to 3.3% on Feb. 1, but left the critical discount rate at 3%. Both the U.S. Federal Reserve and the Bank of France are making bigger cuts, however, so the Buba may have to make a splash move soon. If not, the mark could rebound and start another downward spiral in Germany's export-dependent industrial sector.

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EXECUTIVE SUITE

INSIDE APPLE'S BOARDROOM COUP

Eleven tense days, a showdown in Manhattan, a new CEO

Gilbert F. Amelio took the hot seat on Feb. 5. On his first day as the new CEO of embattled Apple Computer Inc., he sent an E-mail, telling employees that he is an "avid" Apple user and that in coming weeks he will meet with them to "begin the process of getting Apple back on track." He sat down with top execs, squelching fears of wholesale firings, and asked for ideas on how to return Apple to health. And he told his top marketing chief: "We must have some good news every day." Says Satjiv S. Chahil, senior vice-president of marketing: "He's just what the doctor ordered."

Now, Amelio has to come up with the right medicine. Credited with reviving troubled National Semiconductor Corp., Amelio already is assessing Apple's ills: slowing sales, shrinking market share, a quarterly loss, layoffs, a painful exodus of executives, and no blockbuster products to bail it out anytime soon.

There's also the question of how to resolve ongoing merger negotiations with Sun Microsystems Inc. On Feb. 7, the two companies were once again bargaining after haggling most of the previous weekend in the Palo Alto (Calif.) offices of Wilson, Sonsini, Goodrich & Rosati, Sun's law firm. It was unclear, however, if the talks were about a merger, an Apple equity position for Sun, or a technology partnership. Why talk now, after Amelio has been brought on board? Insiders say there was no deal in sight when Amelio took the job but that Apple board members haven't given up their interest in a pact—as long as the price is right. Though talks continue, insiders at both Sun and Apple are skeptical that a merger will come off now.

Nobody knows exactly what Amelio will do to revive Apple. But insiders think he is mulling an approach like the one he took at National and the one Louis V. Gerstner Jr. took at IB[illegible] Say little, listen to employees, cu[illegible] tomers, and dealers. Then come o[illegible] swinging.

At least Apple is clear of the hyst[illegible] ria zone—the weeks of tumult betwe[illegible] doses of bad financial news, rumors [illegible] the Sun deal, and shareholders calli[illegible] for the head of CEO Michael [illegible] Spindler. On Feb. 2, they got wh[illegible] they wanted. Spindler resigned, a[illegible] Amelio, an Apple board member f[illegible] 15 months, steppi[illegible] in, ending one of t[illegible] most bizarre cha[illegible] ters in Apple's high-drama histo[illegible]

This chapter involved boardroom th[illegible] atrics at its best. It began on Jan. [illegible] the day of Apple's annual shareholo[illegible] meeting. Board members and Spind[illegible] were expecting tough but manageab[illegible] criticism from investors. Insiders s[illegible] Spindler and the board had begun se[illegible] ous negotiations to sell Apple to S[illegible] the week before, and a deal looked lil[illegible] ly. All they had to do was weather t[illegible] meeting.

TURNAROUND-ARTIST SHUFFLE

1985-93

John Sculley

1985 REVENUES	$1.9 BILLION
PC MARKET SHARE	8.7%
GROSS MARGINS	42%

OUTCOME CEO Sculley ousted Steve Jobs in '85, then cut 1,200 people and took a $40 million charge. A new Mac, the LaserWriter-Plus, and other products drove up sales. Gross margins rose to above 50% by early '86, and the stock more than doubled by midyear. By '93, though, price wars and heavy R&D spending got Apple in trouble again.

1993-96

Michael Spindler

1993 REVENUES	$7.9 [illegible]
PC MARKET SHARE	[illegible]
GROSS MARGINS	[illegible]

OUTCOME Spindler laid off 2,[illegible] people, slashed costs 13%, a[illegible] product prices by 30%-plus. [illegible] harsh measures, plus Macs b[illegible] on the new PowerPC chip, g[illegible] company a sales boost by mi[illegible] But Apple misjudged the ma[illegible] and couldn't meet computer [illegible] demand in '95. Losses and m[illegible] layoffs ensued.

Spindler was coached on how to take
icism without responding angrily,
ders say. That would prove handy,
ne jab after another was thrown at
. Afterward, at a press conference,
irman A. C. "Mike" Markkula Jr.
ported Spindler, even patting his
ulder and telling the press: "I like
guy. He's a very good person."
ut events would quickly erode
kkula's backing. That afternoon, the
rd met to consider Sun's merger of-
On the table: a proposed stock
p, valuing Apple's shares in the
-20s—far below its 31¾ selling price
t day. The board was stunned.
reholders were unlikely to approve
a lowball bid. Says one insider:
e board really thought they would
e out with a deal and all would be
iven."

SHING NEWS. Realizing a merger
now dicey, the board met again
night for a "business session" in
ch one Apple executive after an-
r made presentations, outlining the
es Apple faced. Insiders say the
d listened, nearly mute, barely ask-
questions. But the magnitude of
le's problems began to sink in. Says
insider: "They got their [minds]
nd the fact that things weren't
ning well."

researcher Creative Strategies International. The final blow: On Jan. 29, Standard & Poor's downgraded some of Apple's debt to "junk" status. Says an insider: "It became clear as time went on that this was about more than having buddies on the board."

It was time for Spindler to go. Markkula called an emergency meeting for Jan. 31 at Manhattan's St. Regis Hotel. Insiders say Spindler, who traveled to New York with his wife, was caught off guard and argued passionately for more time. The board was firm: Spindler had contributed much over his 16 years at Apple, but directors had been surprised by plunging gross margins, throwing into question management's credibility. "I know it's the pits, for Michael and for all of us," Markkula stated in a Feb. 4 E-mail to Apple employees. That night, Markkula and Amelio, close friends and both pilots, flew out of New York in Markkula's Falcon 900. Amelio, 52, an engineer with 16 patents, had become Apple's fourth chief.

By 6:30 a.m. on Feb. 1, Apple was aswirl with rumors of Spindler's ouster. Employees scrambled to find copies of their new boss's book, *Profit from Experience*, a step-by-step description of how Amelio "transformed" National Semiconductor from its worst loss ever ($151.4 million in the fiscal year ended May 26, 1991) to its best year (a $264.2 million profit in fiscal 1995).

By Thursday afternoon, Amelio notified National Semiconductor that he was leaving. The news surprised the chipmaker's board and top executives. "I was shocked and annoyed," says Charles E. Sporck, a board member and former CEO and president. "I'm disappointed that he decided to bag it." Amelio met with his seven-member executive committee and National's general counsel late Thursday. In a 20-minute meeting, he assured everyone he had not sought the Apple job. But he said he could not turn down the chance to save Apple. "Gil sees this as a mission for America," says Modesto A. Maidique, a National board member. Since the stock market had already closed, National decided to announce Amelio's plans early Friday morning. But Apple still wasn't ready. So at 8:30 a.m. Pacific time, National finally put out a terse release on its own, saying Amelio had resigned. Apple's announcement came at 6:45 p.m., apparently held up while Spindler hammered out his compensation

Gil Amelio

996-?

VENUES	**$11 BILLION**
ET SHARE	**7.8%**
IARGINS	**15%**

GES Market share and
rgins are way down, and
g new products, such as
nd Copland, won't kick in
Hot-button tasks: Hawk
0 million in inventory and
ctions of key execs.

A: COMPANY REPORTS, DATAQUEST INC.

or seven days, the pressure mount-
Board members, still stinging from
shareholder meeting, were stunned
an onslaught of bad press. Big
eholders, reading leaks about the
talks, began contacting the board
ctly, denouncing the bid. Then,
hing news: Some corporate buy-
worried about Apple's future,
e delaying purchases; a few were
considering a switch to rival PCs,
Tim Bajarin, president of market

package. Apple declines to comment on the matter.

That Friday, Spindler cleaned out his office as his tearful support staff looked on. By evening, the German-born executive sent an emotional E-mail message to Apple employees that began: "Dear Colleagues: The end of a long voyage. A page in my life has turned..." He reminisced and took the full brunt of what had gone wrong. "So it's time for me to go!" he wrote. "Mistakes or misjudgments made? Oh yes—even plenty. Both in business and personal judgment terms. I take personal responsibility for things that didn't work and should have worked. I tried to give it my best—both intellectually and physically in every corner of the world to carry this cause and its color."

Amelio is already plowing through Apple's problems. He hates talk of a "turnaround" because it implies a quick fix with lots of layoffs. He prefers to be known as "transformation manager"—someone who works with employees craft a vision and rally the troops hind it. "He's not a guy who comes and turns things around by swingin machine gun," says Frederick Zieber, president of Pathfinder I search Inc. in San Jose. Whate methods he employs, he faces some the most daunting challenges of a Apple CEO yet.

By Kathy Rebello, with Rob D. Hof and Peter Burrows, in S Francisco

DEALS

PACKARD BELL AND ZENITH DATA: THE TORTOISE AND THE TORTOISE?

It looks like a good fit, but analysts are generally sour

From scratch, Beny Alagem built Packard Bell Electronics Inc. into a $4.5 billion PC company in just 10 years. Trouble is, he keeps having to shore up its foundations.

In a complex, nearly $700 million deal announced on Feb. 7, Packard Bell said it is taking over Zenith Data Systems Corp., a unit of France's Groupe Bull. In exchange, Packard will grant Bull, which already owned 20% of Packard, preferred shares worth up to $400 million. At the same time, Japan's NEC Corp., which also holds 20% of Packard, said that it would pump an additional $283 million into the PC maker, also in exchange for redeemable preferred shares. Voting control of Packard will remain in the hands of Alagem and other insiders.

PHASE TWO? On the surface, Zenith and Packard look like a good fit. Packard is the leading seller of PCs through U.S. mass market retailers and has just begun selling to commercial accounts through traditional computer dealers. Zenith sells almost exclusively to companies and government agencies. Zenith makes notebook computers and network servers, higher-margin products that Packard Bell does not offer. Further, more than half of Zenith's estimated $1.3 billion in sales are overseas, where Packard Bell did less than 10% of its business last year. "What you're seeing is the beginning of the second phase of Packard Bell's growth," says Alagem, Packard's CEO.

There's just the little matter of financial trouble at both companies. "Bad money after bad money is what I would call it," says Kimball H. Brown, an analyst at market researcher Dataquest. Zenith lost more than $100 million last year, according to a company insider. Once a major player in notebook computers—it sold one out of every five portables in 1989—Zenith has seen its market share fall below 3%. One problem: It was late in offering a version based on Intel Corp.'s Pentium chip. And its major government contract, a $700 million deal supplying desktops to the Air Force, has pretty much run out. Bull has been looking for a buyer for the subsidiary for more than a year, so it welcomed Alagem's offer to consolidate it into Packard Bell.

Alagem won't confirm that Packard Bell lost money in 1995, as analysts contend, but the company is showing all the signs of being in trouble. Wa Street believes it is strapped for cas which makes a public offering an u tenable option. Hitting up partners f cash infusions is the company's be recourse for funding growth. NEC new investment brings its total co tribution since August to $453 millio And in November, Intel disclosed tha it had converted part of one cu tomer's $470 million accounts-receiv able tab into a loan. Analysts say th customer was Packard Bell.

TOUGH YEAR. Another big downe The Christmas selling season did n meet Packard Bell's projections. As result, in January, it laid off 250 em ployees at its Sacramento plant, abou 6% of the workforce there. Worldwid its sales were up 35%, to $4.5 billio But analysts say Packar bet heavily on Intel's 7 megahertz Pentium chip an got caught with excess in ventory that it had to u load at fire-sale price Alagem has repeatedly an vehemently denied such r ports: "All the rumor you've heard about our i ventory of Pentium 75s ar totally fabricated," he says

This year could be eve more demanding. Th growth of the U.S. PC ma ket will slow to 16% fro last year's 22%, according t researcher Internation Data Corp. Plus, there wi be tough competition from such co panies as Hewlett-Packard Co. an Acer America Corp.

Still, Packard Bell has gone to th brink and back at least twice in th past three years, and the irrepres ible Alagem thinks he'll bring it bac again. "Now, we have a complete glob al enterprise," he beams. Brave tal Time to make good on it.

By Larry Armstrong in Los Ang les, with Peter Elstrom in Chicag and bureau reports

ANATOMY OF A PC MEGADEAL

Bull transfers money-losing Zenith Data Systems to Packard Bell and assumes some debt in a deal valued at $400 million.

NEC invests $283 million in Packard Bell. It and Bull receive nonvoting preferred stock for their investments, keeping their stakes in Packard at 20%.

Packard Bell becomes the U.S.'s top seller of PCs, as well as gaining Zenith's substantial overseas operation.

DATA: COMPANY REPORTS

BREAKTHROUGH
I THE SKY

e U.S. and Germany are near a landmark reg-slashing deal

ess than five years ago, unfettered international airline competition seemed a hopeless fantasy. Then, in 2, the U.S. struck a deregulation t with the Netherlands. Last year, it similar accords with nine small Euean nations. Now, U.S. and German ation officials are close to reaching t could be a landmark reg-slashing l: an "open-skies" pact that would ually end restrictions flights between the nations—and posy usher in a new era North Atlantic air vel.

he agreement could ease air traffic been the U.S. and Gery by 10%, industry government analysts mate, and generate extra $200 million in ual revenues for erican carriers. Airsources say it could l to new Germaned flight connections destinations in Asia Africa. Most impor., it could pressure -resistant Britain and nce, among others, comparable pacts.

nder the terms ked out in six ths of closed-door otiations between the U.S. Transation Dept. and the German Trans. Ministry, carriers from both couns would be free to set their own s and flight schedules, according to officials. While the agreement ld not allow Lufthansa, for example, ly between U.S. cities, it would t the carrier access to any U.S. ort that maintains customs and imration services. "This is a breakugh agreement," says Matthias mann, Germany's Transport Minis"We've set a flight path to deregula." Announcement of a final deal is cted later this month.

hy now? German aviation officials the pact will help Lufthansa counrivals such as British Airways PLC, h sources say is close to nailing n a partnership with American Air Inc. That deal faces several hurdles: U.S. transportation officials are threatening to block it unless Britain grants U.S. carriers greater access to London's Heathrow Airport, Europe's busiest. If it flies, though, the pact would allow American to feed domestic U.S. passengers into parts of BA's global network, and vice versa, creating the largest and most powerful airline alliance in the world. It also would threaten BA's troubled relationship with partner USAir.

AIRLINE OFFICES IN MUNICH: *For U.S. carriers, the pact would make Germany a major gateway to Asia*

Lufthansa entered into a similar joint operating agreement with United Airlines Inc. in 1994. That alliance would be dramatically strengthened by an exemption from U.S. Justice Dept. antitrust restrictions, which German negotiators are demanding before they agree to open skies. The exemption would free the airlines from laws prohibiting collaboration on fares and coordinating schedules. As a result, Lufthansa and United could realize efficiency savings totaling $40 million, some U.S. analysts estimate. "It's a win-win situation for both airlines," says Lorne Campbell of Schröder Münchmeyer Hengst & Co., a German investment bank.

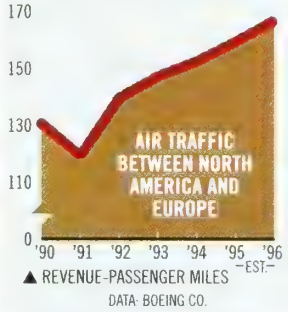
The prospect of a stronger United-Lufthansa alliance is already redrawing the competitive map. American Airlines has ended its flights between Chicago and Munich, saying it cannot compete against the potent combination. For its part, American is calling on U.S. negotiators to speed up talks on gaining more route rights in Japan.

BUSIEST HUB. Transportation Dept. officials, meanwhile, are eyeing Britain and France. Heathrow now handles as much as 70% of air traffic from the U.S. to the rest of Europe. But British authorities have only granted landing rights there to just two U.S. carriers, American and United. The U.S. envisions a deregulated Germany siphoning off traffic from Heathrow and turning Frankfurt into a major gateway to the booming Asian markets. "Is it realistic to think German airports will provide key gateways to the rapidly expanding Asia-Pacific market? Absolutely," says Senator Larry Pressler (R-S.D.), a key negotiator for the U.S. in talks with Germany.

The British scoff at the U.S. gambit to leverage such a deal, and say there simply is no space at Heathrow for more American carriers. British Airways spokesman Michael Blunt says the idea that British Airways officials are afraid to compete against leaner and meaner American rivals "is absolute codswallop." But on Feb. 7, British Foreign Secretary Malcolm Rifkind declared his willingness to reopen U.S.-British aviation talks, which stalled in October. "Last year, we made some progress before talks broke down," Rifkind says. "There's no good reason not to resume those talks." And now there's a very good reason to do so: Germany.

By Christina Del Valle in Washington and Paula Dwyer in London, with Karen Lowry Miller in Bonn and bureau reports

PACKING 'EM IN



PHONE HOME A Nynex service call in New York; long-distance carriers, cable companies, and others are eyeing the local market hungrily

TELECOMMUNICATIONS

HOLD THE PHONE— IT'S A MARKETING FREE-FOR-ALL

The opening of local service will bring a flood of sales pitches

Brace yourself. If you're fed up with phone company ads, never want to hear another pin drop, think you'll yank the thing out of the wall if you get one more call from a long-distance telemarketer during dinner—you ain't seen nothing yet. Congress' Feb. 1 passage of the Telecommunications Act of 1996 is about to unleash a torrent of marketing campaigns importuning you to change something you probably never thought much about before: local phone service.

The landmark legislation, scheduled to be signed into law by President Clinton on Feb. 8, will open up local calling to competition for the first time in decades. It will take six months or so for federal rules to be worked out, but by the end of 1996, consumers across the U.S. should be able to ditch their local monopoly in favor of AT&T, MCI, Sprint, a cable company, or an out-of-state local phone company.

NEW TERRAIN. The pitch? Bundling. Phone companies figure that customers really want a single source for all their communications needs, be they local, long-distance, international, wireless, online, cable TV, or other services. The idea, though, is unproven. In a recent survey by Mercer Management Consulting Inc., just 6% of respondents said they would consider buying all of their services from one company.

Then again, nobody has had the option before. "We believe that if each service in and of itself is of high value, then single-stop shopping is a strategy that can work," says Joseph P. Naccio, executive vice-president for AT&T's consumer business. And carriers may offer some steep discounts on parts of the package. "When I look into the future, I see local service in some cases given away for free," predicts Sprint Corp. policy chief John R. Hoffman.

For now, companies such as AT&T and MCI Communications Corp. will have to lease c ing lines from local phone com ny in order to p vide service. I most plan to swi to an alternat network quick That's when life get confusing consumers. Cho ing a long-distance carrier mainly volves price comparisons. But with lo service, consumers could opt to plug phone into the cable-TV outlet, now t major cable operators are upgrad their networks to offer phone servic

WIRELESS WORLD. If that's not appe ing, there's wireless. Sprint's first wi less network using new personal co munications service (PCS) technology up and running in Washington. The c rier expects to be offering the service 15 states by yearend—for a basic fee $15 a month. AT&T also plans a natio PCS service by mid-1997 and has stro ly hinted that it is prepared to bu its own local wired lines in some are MCI has built local fiber-optic netwo in 25 cities.

The Baby Bells have their o strategies. Once new rivals enter th local markets, the new regs allow Bells to offer long-distance servic which—you guessed it—they plan bundle with other options such as ce lar calling. They may also improve th images. "No more putting customers hold when they call," pledges Brian Lane, marketing vice-president Nynex Corp. "Our service quality sho improve dramatically, and that's the b marketing strategy."

Phone company executives routin say they don't want to inundate c sumers with ads and telemarketing ca But let's face it: Brand awareness become crucial in a market where so 30% of consumers s think they get lo phone service fr AT&T. (No one doe Notes Thomas Elliot managing partner w Arthur Andersen & "For the first time, t industry is going have to communicate

Groan. Get ready take your phone off hook during dinnertim

By Catherine Ar in New York, with M Lewyn in Washingto

ASSAULT ON THE BABY BELLS

Long-distance companies' marketing plans

AT&T Will initially resell local service purchased from local phone companies. By mid-1997, it will market mobile-phone service, too. Other services: satellite TV, Internet connections.

MCI Has built local calling networks in 25 cities, but it still needs a link to individual homes. To get that, it also will start to resell local phone service. Other services: paging, satellite TV.

SPRINT Has partnerships with three cable-TV operators and Teleport, an alternative local phone company that by yearend will offer consumers phone service over their cable lines. Other services include digital wireless calling.

S THERE REALLY ROOM AT THE INN OR STEVE BOLLENBACH?

lton's new CEO still has to answer to the chain's patriarch

tephen F. Bollenbach likes fast cars and the California coast. Barron Hilton favors Cuban cigars and m service at the Hilton-owned Wal- f Astoria in New York City. They 'n't hang out together much. Strange corporate bedfellows, indeed. t there they were, chatting amiably id the cigar smoke in Hilton's Bever- Hills office. On Feb. 5, Bollenbach gan his new job as Hilton Hotels rp.'s chief executive officer. Replac- 68-year-old Barron Hilton, who remain chairman, Bollenbach, became the first non-Hilton head the 50-year-old, $1.7 bil- hotel and gaming empire. How long the ex-surfer and the rician can co-exist is one's guess. Hilton Ho- is a chronic under- former, plagued by indecision of its irman. Bollenbach strong, forceful cutive. For now, ey're on their neymoon," says ney manager rio Gabelli, who ds about 5% of ton shares through ious funds. "After the 100 days, who knows?"

CK AND FORTH. During years at Hilton's helm, ron Hilton, the son of pany founder Conrad N. ton, has forged a tortu- path. He has twice put company up for sale only to renege, torn by his emotional attachment to the family business. He considered, then rejected, a spin-off of Hilton's gaming operations late last year. And he has frozen out executives who wanted to make changes too fast, say insiders. Hilton's stock has suffered as a result: Before jumping 21% in two days on word of Bollenbach's appointment, shares were stuck around 60, no higher than they had been in 1989 (chart).

Enter Bollenbach, a sure-handed financial executive with a solid rep on Wall Street. He engineered a $2.6 billion recapitalization of Holiday Corp. in 1986 and a massive spin-off at Marriott Corp. seven years later. In between, Bollenbach saved Donald Trump's skin, coaxing banks into a restructuring deal that allowed Trump to hold on to his Atlantic City casinos in 1990. And last year, as chief financial officer of Walt Disney Co., he negotiated the $19 billion acquisition of Capital Cities/ABC Inc. "There isn't a blemish on his record," says Joseph V. Coccimiglio, an analyst with Dean Witter Reynolds.

"TREMENDOUS UNCERTAINTY." Industry sources say Bollenbach left Disney because CEO Michael D. Eisner brought in superagent Michael Ovitz as president, diluting Bollenbach's power. Bollenbach denies that, pointing instead to the chance he will have at Hilton to run his own show. "My job is to get involved in the operations and get performance to a higher level," he says.

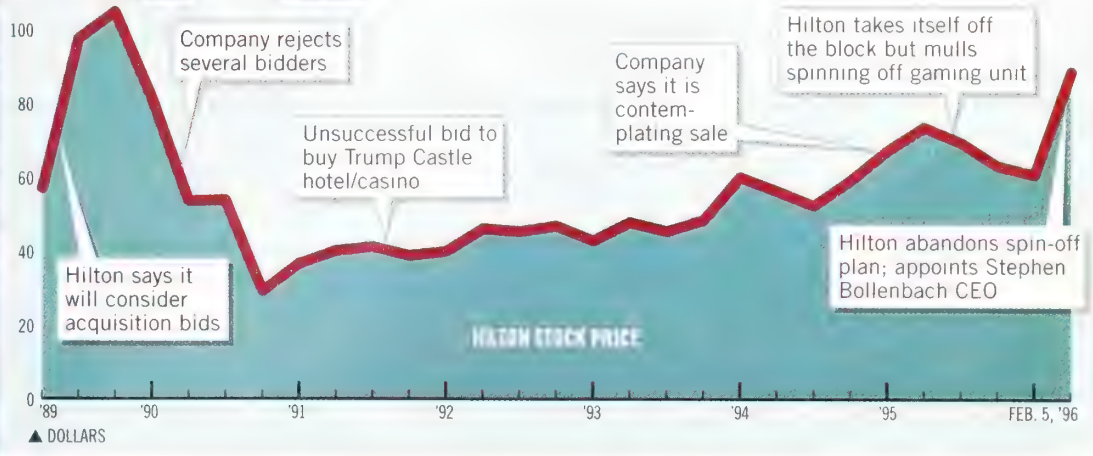
Will he really get the chance? Barron Hilton says he intends to retire to his 550,000-acre Nevada cattle ranch to spend more time flying his fleet of antique airplanes. But to keep tabs on Bollenbach, "I'm going to keep a cell phone with me wherever I go," jokes Barron.

Ominous words, perhaps, for Bollenbach, a man with much to do. Despite 240 hotels worldwide and a strong Las Vegas gaming presence, Hilton needs a boost. Its return on gaming assets was 4.9% last year, about half that of competitors Mirage Resorts Inc. and Harrah's Entertainment. The hotel businesses are faring better: 1995 operating profits were $208 million, up 41%. But investors and other critics charge that Hilton's long-enduring cachet has faded. More important, it badly trails competitors in the fast-growing midprice market for business travelers, while international expansion has been slow. "There's been tremendous uncertainty at Hilton," says Fred Malek, chairman of Thayer Cap-

HILTON HEAD

Ex-Disney CFO Bollenbach, who negotiated the Capital Cities/ABC deal, is known for his dealmaking skill, but he'll have his hands full at the troubled hotelier

Hilton's Elevator Ride



ital Partners and a former president of Marriott Hotels & Resorts.

Bollenbach must persuade Barron Hilton, who still holds 33% of the company's shares, to support decisive action. Most likely, the new CEO will first address Hilton's gaming strategy. His second day on the job, Bollenbach flew to Las Vegas to tour the Flamingo Hilton and Las Vegas Hilton casinos. Those casinos, after face-lifts costing a combined $200 million, are performing nicely. But they're old-fashioned resorts with little room for expansion, and such rivals as Mirage and Circus Circus Enterprises Inc. are spending lavishly to build megapalaces down the street.

More problematic is Atlantic City, where Hilton has repeatedly failed to follow through on plans to enter the resurgent gaming market. Some analysts predict that Bollenbach will use Hilton's strong balance sheet to muscle onto the Boardwalk by purchasing a Bally's or Trump property. And Bollenbach will have to address a series of missteps in smaller, soft markets, such as Kansas City and New Orleans, where Hilton owns a middling riverboat casino.

MEDDLER. Similarly, Bollenbach needs to push Hilton's hotel unit to exploit new markets. Overseas operations are slated to grow from 6 to some 25 by 2000. Meanwhile, Hilton plans to blanket the country with its new Garden Inns. Dieter H. Huckestein, president of the hotel division, plans to plunk down about 100 of the midprice hotels near the popular Courtyard by Marriott locations, slash prices, and offer more amenities.

Strategy is one thing. Dealing with the unpredictable Barron Hilton is another. Industry insiders say the chairman has alienated aggressive and talented senior managers before with his meddling conservatism. In 1993, after failing to persuade Hilton to expand into Atlantic City, gaming unit chief John V. Giovenco left to head ITT Sheraton Hotels. For the next few years, Barron Hilton relied heavily on then-Hilton President Raymond C. Avansino Jr. But insiders say Avansino departed without making much of an impact.

Will Barron Hilton make room for the new guy? "He's the boss, he's in charge," says Hilton through a cloud of pungent cigar smoke. "I want to fly airplanes while I'm still young enough." But one day, Hilton may land to find that Bollenbach has leveraged the company or diluted the family stock holdings. If that happens, the sparks will fly. The honeymoon may be over.

By Eric Schine and Ronald Grover in Los Angeles

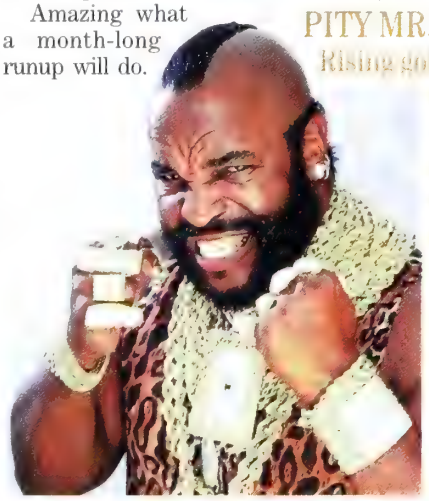
COMMODITIES

WHY GOLD'S FLASH WON'T LAST

Prices are rising, but the upside is limited

For two years, Lucille Palermo struggled as the price of gold went nowhere. Her Van Eck Gold Resources Fund underperformed stocks by 17 percentage points in 1994, then by 33 points last year. But today, her faith in the precious metal has been revived: "We've definitely turned the corner. This is a long-term bull market," she says.

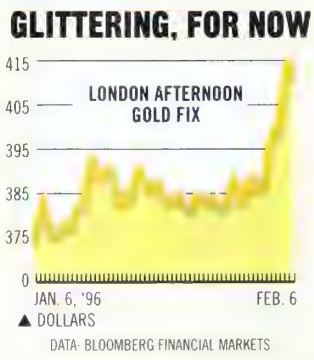
Amazing what a month-long runup will do.



PITY MR. T

Rising gold prices are driving up jewelry costs for consumers. That will eventually undermine demand

Spot prices for the metal have jumped 7% in 1996, closing at $414 per ounce on Feb. 7. That's paltry next to gains of high-flying commodities such as coffee, which has soared 27% in the same period. Yet even a small move in gold has an outsized impact on investor psychology, and on stocks: Palermo's fund, typical of others specializing in gold-mining stocks, was up 27% for the year through Feb. 6.



DUMPING HOARDS. This party probably won't last long, though. In the absence of runaway inflation, a financial meltdown, war, or political crisis, the metal's potential upside likely is limited. Many, indeed, believe that gold has already seen its best days this year: "We're in the eighth inning," cautions analyst J. Clarence Morrison of Prudential Securities Inc.

True, the fundamentals seem compelling. Demand for gold for jewel electronics, and investments soared 1 last year—much of the increase comi from India, where gold remains a vored storehouse of value. Mine pr duction, meantime, declined for the s ond consecutive year. "The physi market provided the launching pad" a rally, notes Stewart Murray, chief e ecutive of Go Fields Mineral Se vices Ltd.

What ignited t rise, though, was big drop in fo ward-selling mining compani Through most 1995, the mines h kept a lid on go prices by extending their use of hedgi programs designed to lock in future se ing prices. But late in the year, cent banks didn't keep up with demand gold supplies used to finance the hed ing activities. Their resulting high rates made hedging less profitable, e ing selling pressure in the market. A Barrick Gold Corp Jan. 30 disclosure plans to cut forwar selling by one-third c firmed the suspicions bullish speculators, w quickly pushed pric higher. The market al drew strength from t robust dollar, the fe eral budget stalema and interest-rate cu at major central bank

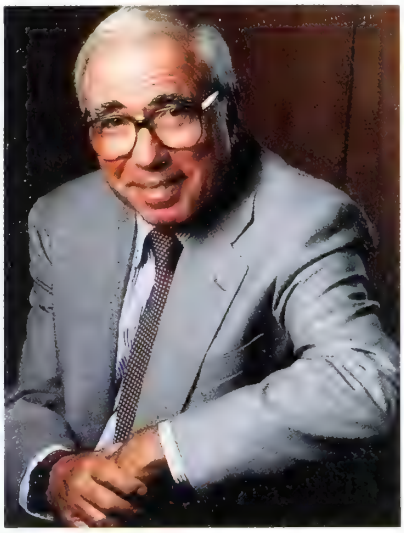
The price increa could quickly unde mine gold's fundamentals. Investors n are likely to dump some of their hoar Consumers will back off pricier jewel while analysts say production will ed up this year. Forward-selling on t part of producers could well ramp again. And gold's best friend—inflation remains indisposed. Ultimately, ther little risk that prices will fall below $3 per ounce. But there's not much upsi left, either. Advice: If you're not i gold yet, stay out.

By Greg Burns in Chica

ELIX AND ALAN: OW THAT'S AN ODD COUPLE

may be fireworks at the Fed if Rohatyn gets the No. 2 post

obody ever said that Felix G. Rohatyn was a inking violet. w, the Lazard res & Co. invest- it banker, who behind such ma- deals as the 0s New York bailout and the 4 employee buy- of United Air- s, is about to e an even more minent role: He's ig to Washing- —if he can win ate confirmation, is.



OUTSPOKEN: *Rohatyn would be a forceful advocate for growth*

ny day now, sident Clinton is ected to nomi- e the 67-year-old financier as vice- rman of the Federal Reserve. The sident's clear hope: that the out- ken advocate of faster economic wth will serve as a counterweight to tight-money tilt of Fed Chairman n Greenspan, whom Clinton also is to renominate.

II QUESTIONS. Given Greenspan's i esteem with Republicans and on l Street, Clinton feels he has to re- inate the Fed chief. But in an elec- year, the President also wants eone on the board to rein in enspan's inflation-fighting tenden- . Outgoing Fed Vice-Chairman Alan Blinder occasionally challenged enspan, and the Administration es Rohatyn will do the same—more n. "If Greenspan thought Blinder a troublemaker, he'll find Rohatyn be much less judicious," says one White House insider.

But first, Rohatyn must win confirmation from a GOP-controlled Senate that hardly shares his liberal views. White House insiders and Capitol Hill lawmakers say Rohatyn will face a tough grilling but is likely to survive. He has the solid support of Democrats grateful for his years as a party fund-raiser. Moreover, the Senate has never blocked a Fed nomination solely on policy grounds.

That doesn't mean the GOP will accept Rohatyn quietly. Senate Republicans probably won't raise a whimper when it comes to reapproving the conservative Greenspan, whose current term expires on Mar. 2. But some lawmakers plan to grill Rohatyn about his past as well as his monetary views and his relationship with the Fed chairman. "The first question we'll have is, 'How well can he work with Alan Greenspan?' " warns Senator Robert F. Bennett (R-Utah).

Another major source of questions is likely to be recent scandals in Lazard's municipal-bond business—an operation the firm built up largely on Rohatyn's stellar reputation from the New York City bailout. Late last year, Lazard agreed to pay $12 million to settle a muni probe in Massachusetts; in 1994, it and Merrill Lynch & Co. anted up $3.6 million as a result of alleged wrongdoing in munis in Washington, D.C. The firm also faces an ongoing Securities & Exchange Commission probe over its muni dealings in Los Angeles. Rohatyn declined to comment for this story.

Rohatyn also may take fire from Western lawmakers. To comply with a law that prevents any two Fed governors from representing the same district, the White House would have to nominate the Wall Streeter not as a New Yorker—which is Greenspan's home—but as a representative of the region that includes Wyoming, where Rohatyn is building a ranch.

POLICY FEUD. If Rohatyn gets on the Fed board, the fireworks may really begin. Never shy about expressing his views, Rohatyn could trigger a major policy feud. "There's potential for a clash of egos," says one Wall Street economist. "I don't think Rohatyn is going to the Fed to be vice-chairman so much as co-chairman."

At issue is the economy's growth potential. While Fed officials—and Clinton's economic advisers—doubt the economy can grow much more than 2.5% a year without rekindling inflation, Rohatyn thinks it can safely expand at a 3.5% clip. The implication of his argument: The Fed is preventing job creation. That's a sentiment that many executives share. "We clearly need some creative thinking as to how we can have faster growth," says Robert L. Crandall, CEO of Dallas-based AMR Corp. "Felix is a very creative guy."

Within the marble walls of the Fed, however, such ideas probably won't wash. Other members of the policy-setting Federal Open Market Committee strongly back Greenspan's campaign to drive inflation sharply below the sub-3% level of the past four years. If outvoted by his peers, Rohatyn may take his case public. "He will play more of an outside game," predicts a Clinton adviser. "He has a big enough name and ego to use the media to cause Greenspan problems." At least, that's what the Clintonites are hoping.

By Dean Foust in Washington, with bureau reports

ON FED POLICY "If the government settles for slow growth through restrictive monetary policy, on top of the fiscal drag from reducing the rate of federal spending by over $1 trillion... over the next 7 to 10 years, the country will incur needless pain and runs the risk of increasing social strain."
(Guest Editorial, U.S. News & World Report, *Aug. 28, 1995)*

ON THE 1980s "We have just seen the end of the greatest decade of speculation and financial irresponsibility since the 1920s.... The junk-bond peddlers and the raiders, the speculators and the savings-and-loan hustlers... turned this country into a vast casino."
(Speech at Northwestern University, February, 1991)

ON REBUILDING AMERICA "The federal government should commit to provide at least $500 billion over the next 10 years... to rebuild America by investing in infrastructure. A 5¢-per-gallon gas tax, increasing over 10 years to 50¢... would generate $50 billion per annum by 2002."
(Op-Ed column, The Washington Post, *July 6, 1992)*

PEOPLE

I'D RATHER BE RICH THAN...

Powell is earning a fortune by not running for President

He's not running for President. And his book just dropped off *The New York Times* best-seller list after a five-month run. But Colin L. Powell is no old soldier fading away.

Since he took himself out of the Presidential sweepstakes on Nov. 8, Powell's political stock—and bank account—have soared. If he maintains his current pace, BUSINESS WEEK estimates that Powell, who charges $60,000 to $100,000 per appearance, may earn $6 million this year from speech-making alone. And Random House Inc. has put 1.6 million copies of his autobiography, *My American Journey*, in bookstores. Powell will start to get an estimated 15% of the book's gross if the publisher recovers the general's reported $6.5 million advance—a possibility this year.

All told, not a bad supplement to Powell's military pension of $90,000 a year.

Powell's routine is to give about two speeches a week, most often to a corporate audience. He spoke to 100 chief executives, for instance, on Jan. 19 at the BUSINESS WEEK President's Forum in Palm Springs, Calif., 2,300 American Hospital Assn. members in Washington on Jan. 29, and an overflow crowd of 800 on Jan. 30 at the Society of Four Arts in Palm Beach, Fla. He talks without notes for about an hour, generally concluding with a powerful call for U.S. global leadership. "He's the most impressive speaker I've heard in 25 years," says Victor L. Campbell, senior vice-president at Columbia/HCA Healthcare Corp.

Despite his appeal to business, Powell hasn't signed on as a corporate director. Rather, he serves gratis on the boards of the Boys & Girls Clubs and the New York-based Children's Health Fund. He's also a trustee of Howard University and plans to join the board of the Ellis Island Restoration Commission.

$6 MILLION MAN

Powell, who routinely gives two speeches a week, charges $60,000 to $100,000 per appearance

Will Powell yet run for President? The general tells friends what he tells his audiences: He's not a candidate this year, though he might run one of these days. The way he's going, Powell may be able to finance a White House bid in the fashionable new way—with his own money.

By Stan Crock in Washington

CHESS

YOUR MOVE, DEEP BLUE

Can chess king Kasparov beat an IBM supercomputer?

Big Blue wants to help science find life-saving drugs, forecast hurricanes, and study galaxies. It wants to divine the economy. First, though, it wants to whip Gary Kasparov's butt.

IBM is into chess. Its Deep Blue supercomputer, the fruit of eight years of research, will take on world chess champion Kasparov in a six-game match in Philadelphia starting on Feb. 10. The winner gets $400,000 from the sponsoring Association for Computing Machinery. No computer has ever beaten a world champion in a standard tournament of unhurried games—but this time, some chess fans are wagering on the machine.

No wonder. Deep Blue is a new sort of supercomputer, based on a standard parallel-processing system called the Risc System 6000 Scalable Power Parallel System. That machine—SP for short—is already pretty fast. But IBM's crew made it go perhaps 1,000 times faster on chess problems by surrounding each of its 32 processors with eight chips hard-wired to do nothing but race through the analysis of millions of chessboard positions. Deep Blue can sort through an awesome 100 million positions per second.

MIDGAME MANEUVERS. The hybrid design has commercial potential, IBM believes. The basic computer can be programmed to handle all kinds of tasks. And when it comes time for a specialized job—drug design, say—the extra chips kick in horsepower on rote tasks.

KASPAROV: *"Mistakes come when you're in a fury or nervous"*

While Deep Blue isn't for sale, similarly customized SP machines could come to market in the next couple of years, prices ranging from $150,000 to tens of millions of dollars.

Kasparov admits to being a little spooked by Deep Blue, especially since the brand-new computer hasn't played any games for him to analyze. He thinks he will win, though, by playing as coolly as the computer itself: "Mistakes come when you're in a fury or nervous. And he believes he'll be able to detect Deep Blue's weak points. A computer, he says, is hamstrung by its inability to adjust its programmed-in priorities during a game. So if Deep Blue is instructed to give top priority to keeping the king safe, it continues to do so even when developments in the game dictate a shift in strategy.

IBM agrees that the inability to learn midgame is Deep Blue's Achilles' heel. So can it win? Chung-Jen Tan, leader of the Deep Blue engineering team, is a bit diffident. "We're pretty confident, but it's hard to tell," he says. Kasparov, typically, is bolder: "My general knowledge of the game and my ability to keep the game under control will eventually prevail." Deep Blue was not available for comment.

By Peter Coy in Philadelphia

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EDITED BY KEITH H. HAMMONDS

A FRUIT FREEZE? PERISH THE THOUGHT

FEAR NOT, TANGELO LOVERS. The South got a bracing blast of winter, but most crops pulled through. As temperatures dropped below freezing on Feb. 1, citrus growers broke out smudge pots to warm their groves, and fruit and vegetable farmers gave their produce a protective layer of ice to fight off freeze damage. Georgia's peaches and pecans escaped the cold spell unscathed. Meanwhile, Florida Citrus Mutual, a growers' organization, expects a reduction in orange-juice yield, but only "moderate" price increases. Indeed, after spiking to $1.32 a pound on Feb. 1, juice futures settled back to $1.20 on Feb. 7. Even if damage turns out worse than expected, "there will be fewer oranges left on the tree, so we'll get more money," figures Orlando grower Jerry Chicone.

CLOSING BELL

CUT TO THE QUICK

There are better lists to make. On Feb. 6, the California Public Employees' Retirement System put U.S. Surgical at the head of its annual ranking of 10 underperforming companies. CalPERS says investors lost 51% on the surgical instruments maker in the three years ended May 31, 1995. But CalPERS might want to reconsider. True, U.S. Surgical stock is depressed. But it soared 8% Feb. 1 on news that '95 profits had quadrupled, to $79 million. Higher margins led analysts to hike earnings estimates.

ANHEUSER GIVES UP SNACKS

SO MUCH FOR BARROOM synergy: Putting beer and snacks under the same roof only left Anheuser-Busch with soggy chips. After shopping its perpetually money-losing Eagle Snacks division since October, Anheuser announced on Feb. 7 that it will close the unit and take a massive $206 million aftertax write-off. "It's extraordinary to take a great trademark and see it die," says PaineWebber analyst Emanuel Goldman. Anheuser will sell four plants to Frito-Lay, the industry giant that helped force Eagle's demise.

EXPORTS TO ASIA TRIM THE TRADE GAP

THANKS TO A ROLLING EXPORT surge, the U.S. merchandise trade deficit shrank 27.5% in November, the fifth straight monthly decrease in the trade gap. That's welcome news for the Clinton Administration, which is getting hammered about the issue on the campaign trail. The big bright spot: exports to Japan, which grew at four times the rate of imports. Exports to China were up 25% in 1995 through November, compared with an 18% increase in imports. Such export strength makes further shrinkage in the deficit likely. Even so, the deficit for the year, in goods alone, stands at a record $162 billion.

SONY: A NEW ROUND OF SWORDPLAY

THE MUSICAL CHAIRS AT SONY America continues. Following the December ouster of CEO Michael Schulhof, Sony parent President Nobuyuki Idei appointed Tadasu Kawai as his personal deputy in the U.S. Now, Kawai's predecessor at the troubled U.S. unit, Executive Vice-President Kyoji Hoshikawa, is being recalled to Japan. Sony Electronics consumer-products marketing chief Yuki Nozoe will join the U.S. unit's top management, concentrating on developing new businesses involving both hardware and entertainment.

HEADLINER: ALBERT COSTELLO

BACK IN THEIR GOOD GRACES

The heat was on Albert Costello. The chairman and CEO of W.R. Grace hadn't delivered a promised spin-off of the company's kidney dialysis unit, National Medical Care. Grace's stock was stalled. Some investors were growing frustrated with a manager one said was "invisible to the Street."

Then came Baxter International's public airing of a $3.8 billion bid for National Medical on Feb. 2. But Costello had a deal of his own. On Feb. 5, Grace unveiled a surprise agreement to combine NMC with a dialysis-supplies business owned by Germany's Fresenius. Grace shareholders would own 44.8% of the new company, plus some preferred shares. Grace itself would get $2.3 billion.

Baxter refused to back off. "We believe that our offer is substantially higher," said CFO Harry Kraemer Jr. in a Feb. 6 conference call. But Baxter needs to up its bid to at least $4.2 billion, Grace execs say, adding that Baxter had lowballed earlier bids. And the pressure seems to be off Costello—for now. "Everything I've told [investors], I've delivered on," he says. "I really want to get on with the damn business."

By Gail DeGeorg

RINGLEADERS FOR THE REVLON SALE

RONALD PERELMAN'S 1992 attempt to sell part of Revlon, his crown jewel, proved an embarrassing flop. A weak stock market and Revlon's perilous debt burden helped kill the offering. But another factor was the confusing profusion of underwriters, eight in all. Perelman has learned from his mistake: This time he has hired 11 Wall Street firms to underwrite an estimated $150 million offering of 15% of Revlon, likely in the next few weeks. But he has also made certain that Merrill Lynch and CS First Boston, the co-lead managers, are running the show. The others, including Goldman Sachs and Bear Stearns, cannot attend due diligence sessions, says one banker. "They just get their name on the front cover of the prospectus, he says.

ET CETERA . . .

- "Mirror, mirror on the wall. . . . You talkin' to ME?" Scorsese signed with Disney.
- Mattel abruptly abandoned its bid to press rival toymaker Hasbro into a merger.
- Fat wins: McDonald's will phase out some salads and the McLean Deluxe sandwich.
- Ray McIntire, the Dow Chemical scientist who invented Styrofoam, died.

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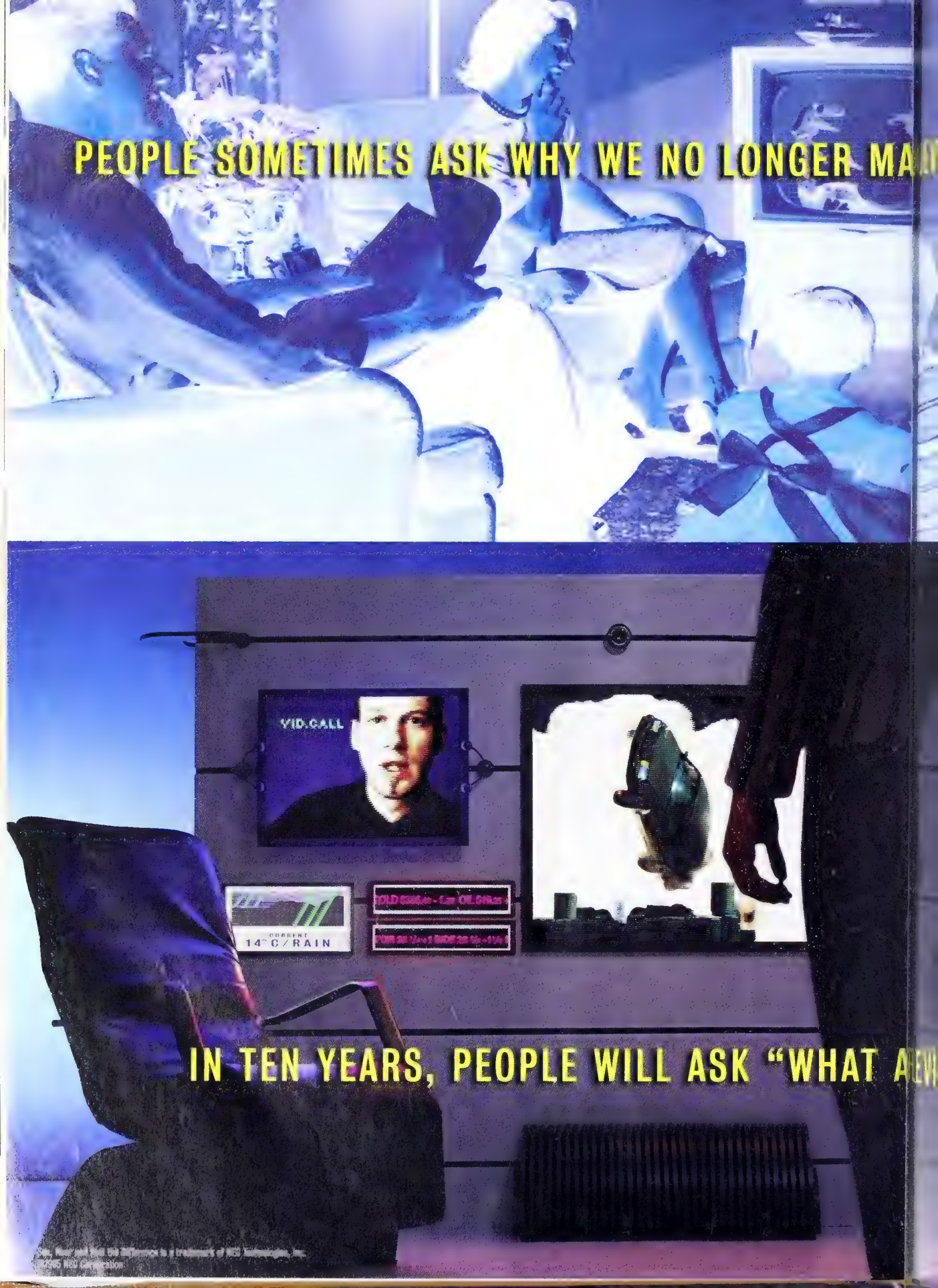
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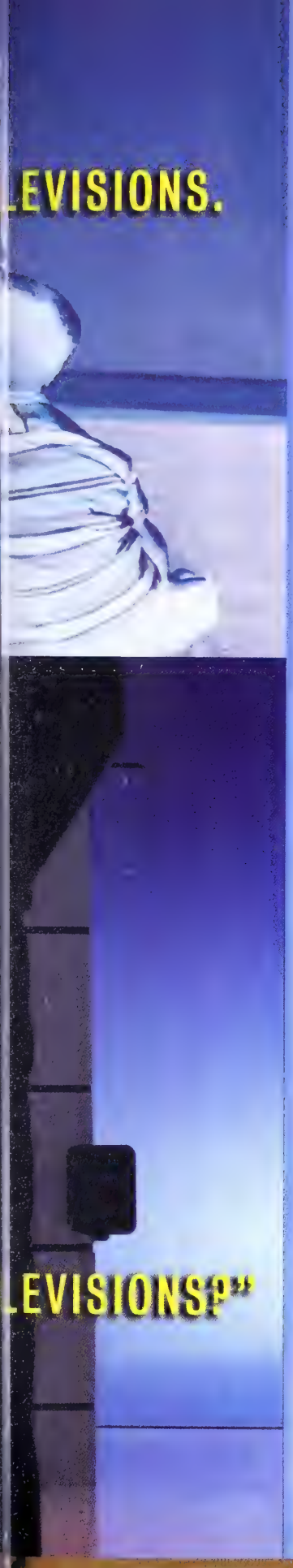

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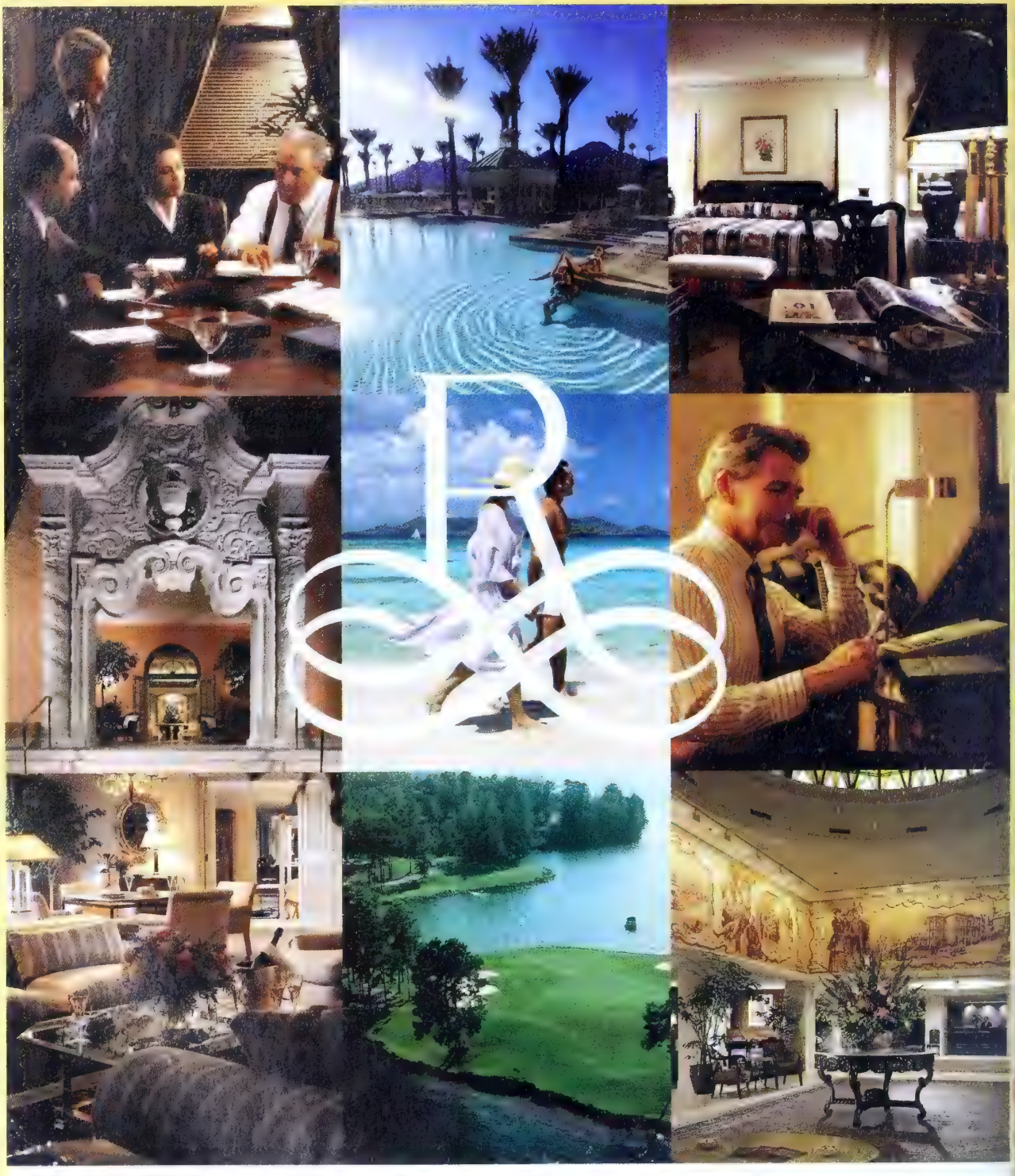

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ITED BY OWEN ULLMANN

REE TRADE: EPUBLICANS MAY BE LOSING FAITH

Ver since Ronald Reagan came to Washington, free trade has been bedrock Republican philosophy. While Democrats lirted with protectionism, the Reagan and Bush Admin-ations launched the North American Free Trade Agree-t, closer Asia-Pacific economic ties, and a global accord to er tariffs—all with broad support.

ut as the '96 campaign unfolds, mainstream Republicans' or for open markets shows signs of cooling, and that has porate America sweating. Exhibit A: GOP Presidential t-runner Bob Dole (R-Kan.), an avowed free-ler and early NAFTA fan, is expressing second ughts, partly because trade with Mexico n't been the big U.S. job creator that backers mised. In November, the Senate Majority der called for a "cooling-off period" on new le deals, a position that put him at odds with se Ways & Means Committee Chairman Bill her (R-Tex.) and other Republicans who favor le's quick entry into NAFTA.

ISENSUS CRACKS. Dole is also pushing for a l escape clause to let the U.S. wiggle out of new World Trade Organization if it tram-on American sovereignty. His idea gained ort in Congress after the WTO, in its first rul-sided against the U.S. on Jan. 17 in a case ught by Brazil and Venezuela.

ole's harder line on trade may be both an election-year and a bow to the new Republican reality: the GOP's flir-n with economic nationalism. Although GOP Presidential comer Steve Forbes remains an unreconstructed free-er, Republican candidate Pat Buchanan has tapped into dle-class economic insecurity with antitrade rhetoric. In-l, he credits his victory in Louisiana's Feb. 6 GOP caucus art to his attacks on multinationals moving jobs abroad. hat's causing the GOP's free-trade consensus to crack. "I a shift to protectionism," laments Representative David ier (R-Calif.), a trade stalwart. Many GOP rank-and-filers blame global competition for America's stagnant wages and vanishing jobs. That sentiment in 1994 helped elect House Republican freshmen who are cooler to free trade. "Once a Wall Street party, the GOP is increasingly a Main Street party," says Paula Stern, a former chair of the U.S. International Trade Commission.

It's little wonder that American companies are on edge, since many see their greatest growth abroad. "There is a deep concern in the business community" about growing GOP protectionism, says the Republican CEO of a major high-tech company. In fact, business already has been disappointed by its GOP allies. On Jan. 26, the Senate approved a bill that would make it easier for Florida farmers to obtain import relief against a flood of Mexican tomato shipments—with little opposition from Finance Committee Chairman William V. Roth Jr. (R-Del.), a free-trader. To the dismay of big business, Senator Alfonse M. D'Amato (R-N.Y.) has co-sponsored a resolution calling for restrictions on Mexican truckers operating in the U.S. And GOP China critics are threatening to scuttle White House plans to renew Beijing's preferential trade status in June.

WAVERING: *Dole backs off*

Business groups gripe that the Senate has become noticeably more protectionist since Senate Finance Committee Chairman Bob Packwood (R-Ore.) resigned. "There is no obvious champion for open trade among Senate Republicans," complains one lobbyist.

Without strong GOP advocates, business can forget about an expansion of NAFTA, a proposed transatlantic free-trade deal, or a new round of global trade negotiations. In the long run, economic globalization may be unstoppable. But if the Republicans' newfound distrust of open markets proves to be more than convenient election-year politics, the next few years could be bleak indeed for free trade.

By Amy Borrus

CAPITAL WRAPUP

FIVE-FIGURE THANK YOU?

President Clinton has a new fan club Lexington, Mass., home of Raytheon Co. According to new Federal Election Commission reports, 22 senior ytheon officials each gave the legal ximum of $1,000 to Clinton's reelection campaign last November. Donors lude Chief Executive Officer Dennis J. Picard, two executive vice-presints, and two senior veeps. Why the gesse? Perhaps because intense Administration lobbying helped Raytheon win a $1.4 billion contract from Brazil in 1994 for an environmental surveillance system for the Amazon rain forest. And in 1995, the Administration fought attempts by a French company to steal the business away from the U.S. electronics giant. A Raytheon official insists the donations "have nothing to do with" the Administration's helping hand.

THE CHINA SYNDROME

▶ The Clinton Administration is telling corporate lobbyists to forget about getting U.S. Export-Import Bank financing for deals in Vietnam this year. The problem: President Clinton must decide whether to expand trade with Vietnam by June, which is when China's most-favored-nation trade status also comes up for renewal. Granting trade benefits to either of the authoritarian regimes will be controversial in Congress, and Clinton doesn't want two fights on his hands, aides say. So he'll take flak for renewing China's MFN status and let Vietnam wait. Lawmakers are upset with Beijing's huge trade surplus with the U.S., weapons proliferation, and human rights abuses.

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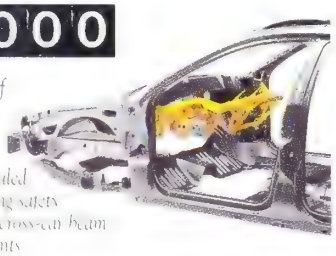

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MARKETS

AWASH IN CHEAP MONEY

Emerging markets are surging

When the stock of Mexico's bankrupt airline, Corporación Mexicana de Aviación, rises 18.5% in one day with nary a smidgen of good news in sight, as it did on Feb. 1, something big is happening.

Mexicana is up because foreign investors—the ones who deserted Mexico in droves as the peso and stock market collapsed in '94 and '95—are suddenly back. They're buying troubled banks and battered builders, too. And they're hardly limiting their sights to Mexico. In fact, American and other overseas investors are pouring cash into the developing world's bourses again (charts). That's sending prices soaring from Warsaw to São Paulo and on to Singapore, where stocks just touched an all-time record.

BUSY PUMP. Of course, there's still no shortage of political concerns to make investors worry—including drug-money scandals in Mexico and Colombia, Russia's leftward drift, and Beijing's saber-rattling over Taiwan. But investors are accentuating the positive because cash is surging into the world economy.

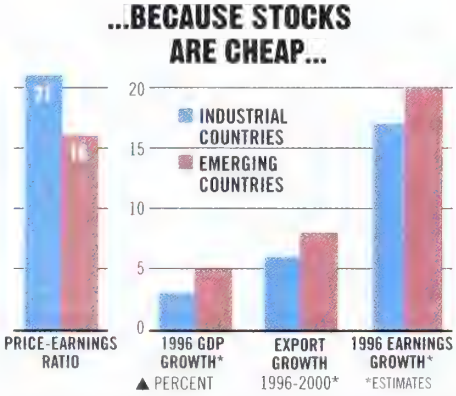
With the German Bundesbank and U.S. Federal Reserve joining the Bank of Japan in cutting interest rates aggressively in recent weeks to spur growth, the global money pump is beginning to work overtime. And even after the stock markets of the industrial world absorb their share, plenty is left over for emerging markets.

Perhaps the cash flow will reverse course—as it did in 1994 and '95—if global interest rates turn up late this year or in 1997. But no one is too worried about hot money flows right now. In the U.S., which sets the trends in global investing, AMG Data Services estimates that nearly $2 billion has gone into emerging-market equity mutual funds since Jan. 1.

The Arcata (Calif.) research firm figures that U.S. investors are now moving $1 billion a week into Merrill Lynch, Morgan Stanley, and Fidelity Investments international equity funds, among others, all of which are big buyers of emerging-market stocks. "Cash flows are incredibly strong," says Mark B. Geist, president of San Francisco-based Montgomery Asset Management, whose emerging-market funds have garnered $50 million since Dec. 31. "Nobody expected the kinds of inflows we've seen thus far in 1996," adds Deutsche Morgan Grenfell's emerging-markets equities strategist, Christopher Wood.

All told, global investors may sh... as much as $50 billion into emergi... market stocks this year, estimates str... egist Michael Howell of ING Baring S... curities Ltd. If the forecast holds tr... that would be the busiest pace sin... foreigners pumped a record $62.4 b... lion into these markets in 1993.

The new flow of cash to the emergi... world will help bolster economic refor... and finance the heavy schedule of p...



izations many countries hope to pull this year. China, for one, has lined up companies for listing overseas. And h many pundits predicting a 30% e in the Tel Aviv stock market this ar, Israel hopes to offer shares in ee state-owned banks. Some 30 Israe- echnology companies are also pre- ing to sell shares.

The new outpouring of emerging- rket shares is likely to find a friend- audience. Not only is money cheap, as BUSINESS WEEK pointed out last (BW—Sept. 11, 1995), many emerg- markets are still a bargain. The rise nterest rates that pricked East Asia's 93 equity market bubble and then nbled Mexico left emerging-country urses with an average price-earnings io of 16, says Smith Barney econo- st John Mullin. But industrial mar- s trade at 21, while the Standard & or's 500-stock index goes for 18.

Two of Mullin's favorites, Hungary l Poland, trade at p-e ratios that are ut half the U.S. level. Partly that re- ts the markets' limited share ros- s, lack of liquidity, and the economic and political risks that go hand-in-hand with new markets. Yet Hungary boasts shrinking budget deficits and may soon become the second Central European nation, after Poland, to earn an investment-grade rating on government debt. And Poland expects to have the best economic growth in Europe this year: 5.5%, after 7% in 1995. It also has some high-growth companies. Suzanne D. Patrick, a vice-president at New York broker Arnhold & S. Bleichroeder Inc., notes that the earnings of Krosno, a Polish glassware exporter, are expanding by 30% a year. Says Kristin Nicholson, research manager at Wood & Co. in Warsaw: "This market is cheap."

In fact, nearly across the board, emerging countries now offer faster economic and profit growth than most of their more developed competitors. There are some notable exceptions, of course. Mexico, burdened by 25% inflation as it tries to recover from last year's peso shock, will be lucky to see 2% economic growth in 1996. It must refinance $22 billion in loans from the U.S. and other allies in 1997 and '98, and any stumbles could panic investors. But many other emerging economies face no such trouble. Notes William W. Priest, CEO of BEA Associates, a big New York-based global fund manager that dramatically stepped up its allocation of cash to emerging markets as 1996 began: "You have a combination of liquidity and rather attractive valuations."

That's certainly true for Brazil, which Richard M. Johnston, managing director of Offitbank in New York, dubs "the China of the Western Hemisphere" for its prodigious industrial output and growing consumer markets. Aracruz Celulose, one of the world's most efficient pulp producers, is trading at only 70% of book value. Yet it's flush with cash and may see earnings grow 14% this year. And despite an 18% price jump since December, "there's a lot of gain left," says Wayne Perkins, research director for Brazil's Bank Norchem.

CHINA BULL. Further big gains may be harder to come by in Asia. But Merrily Chiam, head of Nomura Research Institute's Singapore office, still expects "a Chinese New Year bull run" in February as overseas investors keep buying Singaporean shares. Indonesia, too, may surge on the back of anticipated 20% earnings growth. And Nigel Webber, Hong Kong-based manager of the Lexington Crosby Small Cap Asia Growth Fund, sees advances for the British colony. Some disagree, but Weber and other bulls argue that Beijing has ample incentive not to stifle Hong Kong's growth after it takes over in 1997.

> To nearly everyone's surprise, U.S. investors are now moving an estimated $1 billion a week into international equity funds

Webber is equally enthusiastic about almost every other country in his region, and that's the case for a growing number of his rivals, too. As interest rates fall across the developed world, investors are again lured by the romance and potential of emerging markets. Whatever the risks, they seem to enjoy what these markets offer.

By William Glasgall in New York, with Dave Lindorff in Hong Kong, Elisabeth Malkin in Mexico City, and bureau reports

JAPAN

'FUJITSU *SHOKKU*' IS JOLTING AMERICAN PC MAKERS

The company's price war has U.S. rivals scrambling in Japan

The Japanese called it "Compaq *shokku*," or shock. In 1992, the Houston personal computer maker brought U.S.-style competition to Japan: It started selling desktop PCs for less than half of what hometown manufacturers had been asking. The result? Other U.S. computer makers quickly caught on, and within three years, American companies drove PC prices down by 37%, helped annual computer shipments triple, and seized one-third of Japan's $12.3 billion market.

PALMTOP DYNAMO: *IBM is positioned best to compete*

It was an American success story—until last year's fourth-quarter earnings. First, Apple Computer Inc. cited plunging earnings in Japan as a primary reason for its $69 million quarterly loss. Then on Jan. 28, Compaq President Eckhard Pfeiffer told Wall Street that gross profit margins for the company sank to 21.7%, from 24.4% a year ago, owing, in part, to brutal price competition in Japan. U.S. PC makers, also hurt by the stronger dollar, are no longer on the fast track. Many of them, including Apple and Compaq Computer Corp., are ditching low-end machines in Japan to concentrate on more powerful, higher-margin PCs and network servers.

BIG TUMBLE. What's eating profits? Americans call it "Fujitsu *shokku*." Japan's biggest computer company is on a tear. The vertically integrated company is determined to grab market share—even selling machines at a loss, since it can easily make it up with profits from semiconductors and telecom gear. That has stirred up market leader NEC Corp., which saw its PC share tumble to 40% last year from a commanding 53.4% in 1992. NEC—also in chips and telecom products—is matching Fujitsu Ltd.'s price cuts and, in some cases, undercutting them.

Fujitsu and NEC can't afford to be shut out of the booming PC business in their own backyard. Market researcher Dataquest Inc. says PC shipments in Japan soared 71% last year, to 5.7 million units. Dataquest expects shipments in the world's second-largest PC market to expand to 7.6 million units this year.

It's Fujitsu's aggressive prices, however, that send shock waves through U.S. companies. Rivals accuse Fujitsu of dumping in its home market. Analysts reckon the company is losing $300 on a $2,000 machine, at a total cost of more than $1 million each day. Fujitsu insists it is selling PCs near cost, not including advertising, distribution, and other overhead. "It's a potential issue for the Japanese Fair Trade Commission," says Masaru V. Murai, president of Compaq's Japanese unit. How long will Fujitsu continue its price war? "Business is survival," responds Fujitsu President Tadashi Sekizawa.

A relative latecomer to the PC mass market, Fujitsu is making up for lost time. The company overhauled its supply networ dumping locally made parts in favor foreign components 20% to 30% cheape It's working: Last year, Fujitsu double its Japanese market share to 18.2%, b coming the No. 2 PC maker. Now, t company says it wants to take 30% the home market and sell 5 million uni by 1998.

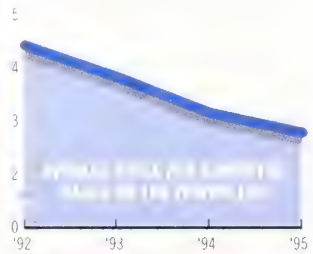
U.S. executives may have starte something they already regret. Tak Apple. Until last year, the company w No. 2 in Japan—it's now third. Ev with lower Mac prices—the Perfor 588 was cut to $760 from $1,615—A ple's share slipped more than a poi in 1995, to 14.2%. John Floisand, cha man of Apple Computer Japan Inc., sa competing on price for market share is no-win proposition. Instead, Apple w focus on higher-margin machines for e ucation, entertainment, and other nich "If you say we're the ones limiting o own ultimate market share with th strategy—so be it," Floisand says.

U.S. HOPE. Compaq didn't fare mu better. Fourth-quarter operations Japan were in the red. The world's lea ing PC vendor boosted its market sha only 0.1 point last year, to a puny 3.8 CEO Pfeiffer now plans to deemphasi low-margin consumer sales and purs higher-margin business PC and serv sales. "We're putting the highest foc on sales of server products; that's whe Japan is moving," he says.

The U.S. company best positioned take on Fujitsu and NEC may be IB IBM Japan Ltd., unlike most U.S. makers, does a lot of product develo ment for the local market, keeping touch with local companies so it can t trends faster than U.S. rivals. Its $2.7 palmtop computer, unveiled in Jap last December, is a good example. was co-developed with Ricoh Co. a Canon Inc., which together built a ti digital camera that slots into the r chine to make it a storage medium still photos, or a video-conferencing s tem. Analysts say has sold 10,000 of t gadgets. Says Kazu Hotta, director of marketing for Japan: "You've got be on the ground bu ing up your bra name." Still, nobody pects an IBM *shok* until the company ready to fight as te ciously as the Japane

Steven V. Brull Tokyo, with Gary Williams in Houston

FALLING PC PRICES IN JAPAN



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FRANCE

THIS FREE-MARKET PROPHET MAY FIND HONOR AFTER ALL

Former Economics Minister Madelin's comeback drive

It looked like a career in ruins. Last August, French Economics Minister Alain Madelin was fired by his boss, Prime Minister Alain Juppé, for publicly questioning why government workers deserved their rich benefits. Pundits took Madelin's sacking as a sign that serious economic reform in France was dead—and that Madelin, politically speaking, was a goner.

But the maverick Madelin refuses to stay on the mat. Six months later, he's back in the news, garnering headlines in *Le Point* and other periodicals as author of a best-selling book and the possible leader of one of France's biggest political parties. And with France's malaise deepening, Madelin's standing as agent provocateur of free-market reform looks likely to grow.

GODCHILD. The 49-year-old Madelin launched his comeback effort on Jan. 30, when he declared his candidacy for the leadership of the center-right Union for French Democracy, the junior partner in France's governing right-wing coalition. An intellectual godchild of Margaret Thatcher, Madelin wants to unify the UDF behind his program to get government out of the markets and to slash public spending and taxes. He also wants private pension funds that could invest in small businesses, which Madelin believes are key to creating new jobs.

Madelin's platform is shaking to the roots a UDF membership divided between free-marketeers and those who back a strong state role in economic planning. Several centrist candidates may still challenge Madelin for the party leadership, so his grab for power is not sure to be successful. But a victory would be an enormous boost for him: The leader of the UDF wields great influence over national legislation, and is usually a serious contender in presidential elections.

But even if he fails to win the UDF post, Madelin has other ways to keep his public profile high. The boyishly handsome politician has gotten himself elected as a representative from a district in Brittany, and he is mayor of the small town of Redon. He is running a think tank, called Idées-Action. And he has just published a book promoting his solutions for France's troubles.

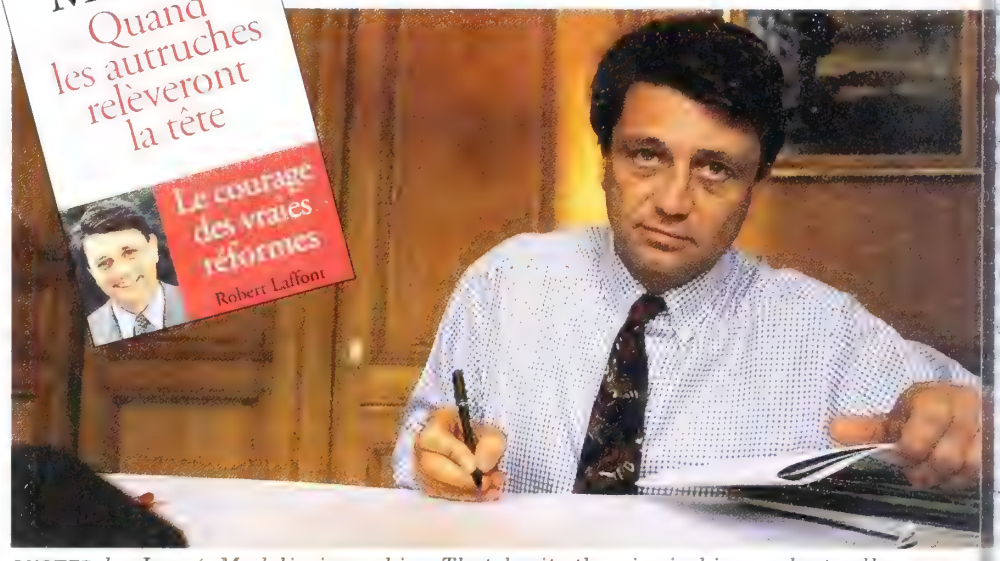
True, Madelin's work, *When the Ostriches Finally Lift Their Heads*, does not offer anything much more radical than standard Thatcherite economics. Yet as France's costly welfare state continues to grow at an alarming rate, Madelin's prescriptions look better and better to the shopkeepers and small-business owners who have been rallying against punitive tax rates, rigid labor laws, and heavy social charges. Madelin, the son of an auto worker, also wants to appeal to the working class, which he says is being overtaxed and overregulated by an elitist political class.

Madelin's quest for more power may benefit from Juppé's own rocky performance. After promising a strong antidote for a paralysis of consumer confidence and a slide toward recession, the best the government was able to come up with was a dollop of Keynesian stimulus, unveiled on Jan. 31. Few expect the plan, which lowers the government-set interest rate on passbook savings and provides new incentives for construction, to make any noticeable difference in the poor economic outlook. A new round of state spending to boost the economy is also unlikely: The government has sworn to contain its swelling budget deficit to qualify for monetary union by 1999.

With France in such a mess, Madelin's critics doubt he could do better than Juppé, should he ever have the chance to put his ideas into action. Juppé in fact did try to scale back civil servant perks—one of Madelin's ideas—shortly after Madelin left the government. A series of crippling strikes ensued. And even supporters admit that as Economics Minister and in an earlier stint as Industry Minister, Madelin displayed disappointingly little skill at implementing even mundane policies, much less the kind of frontal assault he envisions for reforming the welfare state.

But Madelin doesn't have to run the country to be influential. He just has to cultivate his image as a hard-thinking realist, the only one with new ideas now that Juppé is paralyzed and the opposition Socialists have no clear alternatives. "Madelin's ideas are going to be dominant," says Morgan Stanley & Co. economist Eric Chaney. "He's in the trend of what is happening in every European country." This is one voice in the wilderness the French will be hearing more and more.

By Bill Javetski, with Mia Trenepi in Paris



OUSTED *by Juppé, Madelin is pushing Thatcherite theories in his new best-seller*

ITED BY STANLEY REED

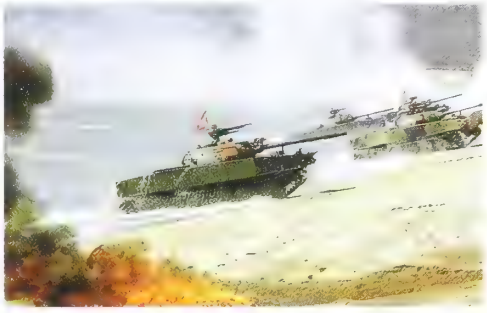
S CLINTON DRIFTING NTO A CRISIS OVER TAIWAN?

Fujian Province, across from Taiwan, tens of thousands f Chinese troops are massing for large-scale military exrcises. These maneuvers are meant to frighten the Taiese electorate into voting against independent-minded sident Lee Teng-hui in the island's first democratic presitial elections, on Mar. 23. But the strategy is backfiring. jing's tactics are helping to make Lee the runaway leader. China's misreading of the mood in Taiwan is just one of a es of miscalculations on both sides that could lead to a gerous confrontation in the coming ıths. Many analysts now believe : if the saber-rattling fails to curb at Beijing perceives as Taiwan's 'e toward independence, China may tempted to take more aggressive on after the election. Lobbing mis- s and disruption of shipping are ı possibilities.

IND THE SCENES. Until very re- tly, the Clinton Administration has med oddly disengaged from the wing tensions in the Pacific—espe- ly considering the enormous prob- that a Taiwan-China fight would pose for the U.S. Now Administration says it is working behind the scenes to id a conflict. Officials say they are reviewing Taiwan's de- sive capabilities, which they describe as "formidable." Americans are also telling Beijing that its belligerence is nating other countries in the region.

But China's near-hysterical reaction to the rise of Lee, Tai- 's first native-born President, is going to make it hard to n the situation. Despite Lee's denials, Chinese leaders ply fear that he is pro-independence. That is heresy in jing, where it is an article of faith that the island, with its 0 billion economy, is just a renegade province. China has ously attacked Lee and his family. "They'll have to deal h Lee Teng-hui," says a China expert in Hong Kong, "but how do you do that after attacking him so personally?"

The Taiwanese have also made some missteps. They have badly underestimated Beijing's sensitivity on the Taiwan question. While something of a diplomatic breakthrough, Lee's visit to the U.S. last year clearly wasn't worth the furor it provoked in China. Beijing shifted to a more aggressive tack that has damaged confidence in Taiwan's economy and slammed its financial markets. "No fund managers want to buy Taiwan stocks," says Huan Guocang of BZW Asia Ltd. in Hong Kong.



MANEUVERS: *China hopes to rattle Taiwan*

One wonders if Lee's government is overestimating the value of the many friends its well-oiled lobbying campaign has won in the U.S. Congress. Could it be that Taiwan is interpreting the praise it hears in Washington for its budding democracy and economic success as a guarantee of U.S. military support?

If so, this is very risky for the Clinton Administration, which may be sleepwalking into a serious foreign crisis. Unlike the Bush Administration, which had plenty of goodwill in Beijing, Clinton's people have virtually no *guanxi*, or good connections, in the Chinese capital. The arrival of former Senator Jim Sasser in Beijing as ambassador after nearly eight months with no top U.S. envoy there may give the U.S. better access. Sasser may also be able to convey how much Chinese human rights abuses and failure to halt ripoffs of software and CDs are hurting China's cause in Washington.

The U.S. is mainly betting that its low-key approach, which somewhat eased tensions with Beijing late last year, will work again. Still, unless Taiwan and China focus more on the price they will pay, their decades-old rivalry may get out of hand.

By Joyce Barnathan in Hong Kong, with Stan Crock in Washington and Margaret Dawson in Taipei

GLOBAL WRAPUP

ERMAN PHONE WARS

British Telecommunications PLC has amed up with RWE, the giant Gerın energy utility, and industrial oup Viag to break Deutsche lekom's stranglehold on the Gerın phone market. RWE brings more an 4,000 kilometers of fiber-optic ca- e, reaching 50% of the German popation, to the partnership. Together, e three companies plan to spend up $2.7 billion over a 10-year period to rest away business and residential stomers from Germany's biggest monopoly, which will be privatized this summer in a $10 billion stock offering. The deal is a coup for British Telecom—which now has a strong position in Europe's biggest phone market. But it means that the group AT&T is trying to put together with Mannesmann and Deutsche Bank—RWE's ex-partners—will face tougher competition.

PEACE CABINET FOR JORDAN

▶ In a move likely to speed improved relations with Israel, Jordan unveiled a new government last Sunday with Abdul Karim Al Kabaritis as the new Prime Minister. In his previous post as Foreign Minister, the outspoken Kabaritis warmly embraced growing ties with Israel, backed up King Hussein's distancing of Jordan from former partner Iraq, and worked to heal relations with Kuwait and Saudi Arabia, former patrons. The new Finance Minister, Marwan Awad, is also seen as a plus because he has private-sector credentials. It is hoped that he will push for the economic liberalization that is badly needed to encourage foreign investment.

POLLUTION

CAN FLOWERS CLEANSE THE EARTH?

Plants hold great promise in waste cleanup

A former Energy Dept. uranium-conversion complex outside Ashtabula, Ohio, is an environmental nightmare, its soil laced with deadly uranium. Cleaning it up would ordinarily mean carting away thousands of tons of polluted dirt at great expense. Now, hope for a better, cheaper approach is blooming—literally. In a small greenhouse on the factory grounds, scores of sunflowers are sucking the uranium out of contaminated water pumped from the soil.

The idea of enlisting nature's flora to cleanse polluted soil is called phyto-remediation—and it's spreading faster than fertilized kudzu. "It's an incredible technology," raves DuPont Co. scientist Scott Cunningham. "Not only does using plants to clean up the world's environmental excesses make sense, it's a heck of a lot prettier than engineering solutions."

NEW NICHE. Cunningham's own experiments show that common crops such as corn or Bermuda grass may be able to yank nearly a ton of lead per acre from contaminated soil each year—just the ticket for lead-polluted DuPont facilities and thousands of other U.S. sites. A variety of plants, including trees, are proving adept at cleaning London sewage sludge, TNT-laden ground at a Tennessee munitions factory, and radioactive fields near Chernobyl. "We are just beginning to explore the possibilities," says University of Missouri biochemist Douglas D. Randall.

Already, a handful of companies—such as Phytotech in Monmouth Junction, N.J., Phytokinetics in Logan, Utah, and Applied Natural Sciences in Hamilton, Ohio—have sprouted to commercialize the new approach. The biggest lure: cost. Burt Ensley, an Amgen Inc. veteran who founded Phytotech in 1993, estimates that plants may do the job of environmental engineers for one-tenth the price. That advantage, Ensley figures, should win him a nice piece of the $12 billion-per-year hazardous-waste-remediation industry. And it could lower costs enough for companies and governments to tackle contaminated areas without prodding from regulators. Insurers, too, are intrigued. Phyto-remediation could be "a significant new strategy," says Stuart Ferguson, vice-president of AM-RE Services Inc., a subsidiary of American Re-Insurance Co.

The big environmental firms are still on the sidelines, waiting for proof that nature can do the job. "We haven't seen enough data for us to go out and apply it yet," says Roger Olsen, vice-president at Camp Dresser & McKee Inc.

Researchers acknowledge that they have more work to do, but they believe convincing data is on its way. Take the progress with heavy metals. Back in 1990, Rutgers University biochemist Ilya Raskin was looking for a biological method to clean up lead, zinc, and other metals. He knew that many plant species can accumulate staggering amounts of these elements, but that most are too small to do much good. So he screened thousands of metal-munching plants before finding a few, such as Indian mustard, that are both large and able to vacuum up metals. Once grown, the plants can be harvested and put into a smelter to recover the metals (diagram) or disposed of appropriately in approved landfills. Even if the metals aren't recovered, the amount of waste—in the form of contaminated plants rather than dirt—is reduced by 98%.

Raskin's work is now being sponsored by $1.2 million from Phytotech. The company's tests in Ukraine suggest India mustard could clean up strontium-laden soils near Chernobyl within five years.

The plants are only part of the story. By adding chemicals that grab on to metals in the soil, scientists can boost uptake a thousandfold. DuPont's Cunningham is trying such a strategy with lead. He uses ordinary plants such as corn or peas that don't normally extract metals and adds chemicals to the soil that flush the lead into the surrounding water. The plants then readily suck up the metal.

GENE-TWEAKING. Genetic engineering promises further gains. At the University of Georgia, geneticist Richard Meagher added a bacterial gene to a mustard relative named *Arabidopsis*. The resulting transgenic plant can take up a dangerous form of mercury from soil, transform it into a less harmful form, and allow it to evaporate into the atmosphere. "Everyone told me it wouldn't work," says Meagher. "But now we have something really spectacular to offer." Scientists are creating transgenic plants that target other metals, too. "The technical breakthroughs in the whole field are coming a mile a minute," says Cunningham.

Still, even phyto-remediation's most ardent boosters admit the technology is not a panacea. Plants won't be able to tackle all sites, such as those where toxins lurk deeper than roots can reach. And since metal-containing plants are themselves hazardous waste, they must be off-limits to grazing animals. Despite these limitations, phyto-remediation still has enormous promise, scientists say. The high-tech cleanups of tomorrow may simply be a matter of letting a thousand flowers bloom.

By John Carey in Washington

AS EASY AS 1, 2

Cleaning up polluted sites that cover a wide area is expensive and time-consuming. Newly identified plants make the process much easier and cheaper.

1 Crops such as sunflowers and Indian mustard, which have been selected for their ability to absorb lead or other pollutants, are planted in contaminated soil.

2 The plants are harvested and discarded in a specially designated site or sent to a smelter where the metals can be extracted and sold off.

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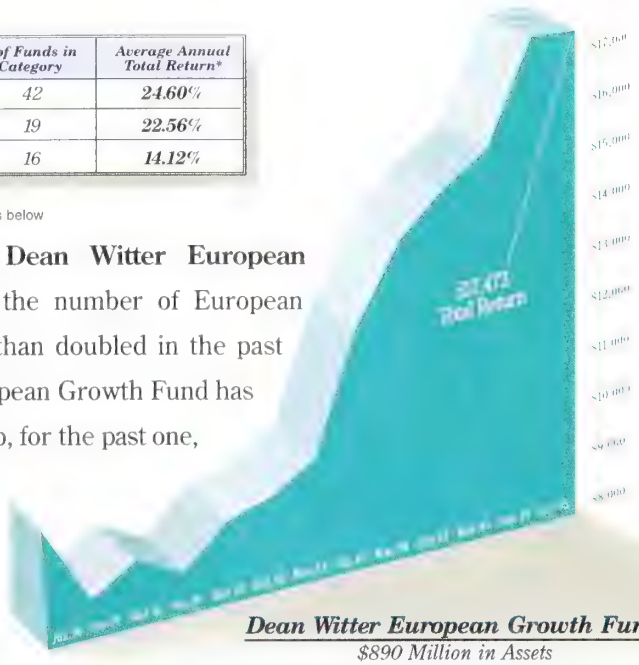

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The above rankings for the 1-, 3-, and 5-year periods ended December 31, 1995, are based on total return and were provided by Lipper Analytical Services, Inc., a leading monitor of mutual fund performance. These rankings did not take into account the fund's contingent deferred sales charge (CDSC), which, if taken into account, might have affected the fund's rankings. The CDSC declines from 5% in the first year to zero after six years and applies only upon the sale of fund shares. The graph illustrates the growth of $10,000 since the fund's inception on June 1, 1990, through December 31, 1995. Dividends and capital gains were reinvested at net asset value, assuming no redemption.

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1996 Motor Trend

Car

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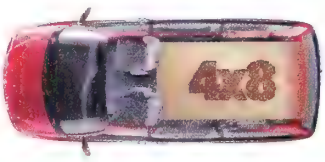

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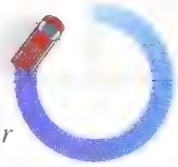

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RESTRUCTURINGS

WHY D&B IS GLUED TO THE TICKER

Wall Street greets a breakup plan with deafening silence

His beeper keeps going off. Dun & Bradstreet Chairman Robert E. Weissman is sitting in his office trying to explain his spin-off strategy, but he keeps getting interrupted. The beeper is signaling yet another story moving over the wires on the company's financial results for 1995.

The news isn't exactly wonderful. Net income was nearly halved, to $1.89 per share, because of a $448 million writeoff for costs associated with a plan to break up the information-services giant. Still, Weissman could also report that revenues grew 10.6%, to $5.4 billion, the first double-digit rise since 1990.

For Weissman, however, even the good news about revenue growth only underlines an unusual problem he believes confronts Dun & Bradstreet Corp.: Its shareholders, who value the company for its high-dividend payouts, are preventing him from more aggressively carrying out a strategy to sustain that kind of healthy top-line growth. His solution: to bust the 155-year-old corporation into three publicly traded companies.

So far, market reaction has been little more than a collective yawn, and some critics say Weissman's novel rationale for the spin-off makes little sense. Unlike AT&T, which saw its stock leap 11% the day of its spin-off announcement, D&B shares continue to languish. As the overall market has reached record highs, D&B stock has risen just 4%, to $66 a share, since Weissman unveiled his strategy on Jan. 9.

The reason: Investors now realize the spin-off disguises a huge cut in the dividend, to about $1.55 from $2.64 a share, and that D&B's market research unit, A. C. Nielsen, is far more beleaguered than previously thought. Locked into a price-cutting war with a tough rival, Nielsen posted only $6 million in net income on $1.3 billion in revenues last year. "Suddenly, people realized how badly it was doing," says Edward J. Atorino, an Oppenheimer & Co. analyst. "Some are skeptical it will show dramatic improvement anytime soon."

Undaunted, Weissman has chosen what is becoming the strategy *du jour*. Breakups are being adopted by a growing number of corporate giants, from AT&T and ITT to Hanson and 3M. Already this year, more than $73 billion in spin-off transactions are pending, up from a record $47.9 billion in 1995, cording to J. P. Morgan Securities In

Studies show that the stock mar rewards a parent company's decision do a spin-off. J. P. Morgan asserts, example, that on average a parent co pany's stock will outperform the mar by 6% by the date of the actual bre up. Spin-offs then outperform the m ket by an average of more than 2 in the first 18 months of independen

Weissman is hoping his strategy w work the same kind of magic. Many today's spin-offs are the result of fai strategies and the market's desire "pure plays." What makes D&B's m different—at least as it is explained Weissman—is the motivation behind breakup: Essentially, he wants to tract a different breed of shareholde The $448 million price tag on this str egy isn't cheap, however, and some gue that its primary purpose could accomplished by better communicati the new growth strategy and follow through on it—all without a cos breakup. "On the surface, this mak no sense," says Thomas Z. Lys, a Nor western University business profess "The managers should do what they b lieve is right and let the shareholde reshuffle themselves."

ANEMIC GROWTH. In one sense, Wei man's strategy is born of frustrati He has presided over a highly pro able company saddled with an aner growth record and a stock that h missed one of the biggest bull mark of all time. Since early 1994, wh Weissman became CEO, D&B stock h eked out a gain of only 5% at a ti when the Standard & Poor's 500-st index rose more than 36%. Reven growth averaged just 1.7% a year si

DUN & BRADSTREET'S OFFSPRING

COGNIZANT

REVENUES $1.4 billion

EMPLOYEES 10,000

KEY UNITS Nielsen Media Research, Gartner Group, IMS International

PITCH TO INVESTORS Potential for high growth

DUN & BRADSTREET

REVENUES $2.0 billion

EMPLOYEES 16,000

KEY UNITS Moody's Investors, Reuben H. Donnelley

PITCH TO INVESTORS High profits, low risks—and low growth

A.C. NIELSEN

REVENUES $1.3 billion

EMPLOYEES 17,000

KEY UNITS A.C. Nielsen market research

PITCH TO INVESTORS Potential turnaround in tough market

DATA: COMPANY REPORTS, BUSINESS WEEK

WEISSMAN: *He wants to attract a different breed of shareholder*

0. Yet the company's return on equi- has averaged 34.2% in the past five rs, nearly four times the profitability Dow Jones & Co. and more than ce that of The McGraw-Hill Compa- s, publisher of BUSINESS WEEK.

What to do? Weissman tried to carve a new image for the not-so-glamor- company based in Wilton, Conn. His t annual report shocked some D&B -timers because it overflowed with tations from trendy management gu- as well as reproductions of abstract More important, Weissman, 55, who ied D&B in 1979, began to focus on enue growth.

D&B's investors were none too ased. When Weissman lowered Wall eet's earnings estimates early last ar so he could invest an extra $75 lion in new-product development and ernational expansion, the decision cost company hundreds of millions in rket capitalization. After Weissman l a key investor that he would pur- revenue growth even if it meant ting D&B's dividend, the stock pped 12%. "Over a billion dollars in rket value disappeared within a week l a half," says Weissman. "That was kind of sensitivity our shareholders l over it. We needed to deal with it."

Ultimately, Weissman concluded that shareholders failed to match up with kinds of diverse businesses that now nprise the company. They think of B as a "preferred stock with modest wth potential," he says. He main- ns that those high-dividend expecta- ns constrained D&B from making larg- investments in businesses with h-growth potential as well as from king defensive investments to shore up units under attack from rivals.

With investment banker Goldman, Sachs & Co., Weiss- man pondered alter- natives, from selling D&B to making a siz- able acquisition him- self—one big enough to transform the en- tire company. No buyer was willing to offer a hefty premi- um for D&B. Gobbling up another company, he figured, wasn't the answer, either. "To the degree you made growth inves- tors happy, they also would say it doesn't look like as much of a growth vehicle as we would like," he says.

Breaking up the company into three parts with different capital needs and growth prospects, Weissman thinks, will make it easier for executives to manage operations and for shareholders to in- vest. Those who like D&B for its stability can keep their shares in the $2 billion D&B spin-off, which includes Moody's. Investors who seek the potential for high growth might find $1.4 billion Cog- nizant Corp. a worthwhile bet. To be headed by Weissman, Cognizant includes health-care market research company IMS International and broadcast ratings firm Nielsen Media Research. Prospec- tors looking for a potential turnaround might go for troubled A. C. Nielsen.

TAKEOVER BAIT? Although investors haven't registered their approval in the market, some shareholders like the breakup. They think the move makes D&B takeover bait. "There is a good likelihood now that one or more of the newly created businesses could be ac- quired," says Mark A. Boyar, who man- ages a $100 million investment portfolio with a stake in D&B. Boyar maintains the breakup value is over $80 a share.

Maybe—but not just yet. Weissman says he is not disappointed that D&B's stock hasn't yet taken off. On the day the board approved the spin-off plan, he told his directors he wasn't sure whether the stock would go up or down. "We believed that if we do this, the val- ue of the company will eventually grow," he insists, just after his beeper sounds a third time. Weissman may have to wait a long time for the beep announcing good news.

By John A. Byrne, in Wilton, Conn.

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INSURANCE

GE SAILS INTO A WHITE SQUALL

Controversy swirls around its insurer's sudden liquidation

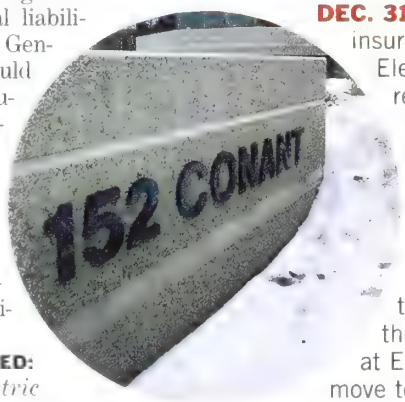
It seemed wholly innocuous, certainly not the sort of move that would stir up an international insurance imbroglio.

At a hearing in Boston last June, David F. St. Laurent, chairman and president of Electric Mutual Liability Insurance Co., asked Massachusetts regulators to allow him to split his company. Insurance policies covering the large and costly environmental liabilities of policy-holder General Electric Co. would remain in Electric Mutual, which would relocate to Bermuda. As a mutual, Electric Mutual is owned by its policyholders, and GE was the largest. The remaining healthy business would be moved to an already existing subsidiary, Electric Insurance Co., which would be spun off as a separate company and stay in Massachusetts. Despite a notice in *The Boston Globe* a week earlier, no one besides St. Laurent and a handful of executives involved in the deal showed up at the hearing. Eight days later, the Massachusetts Insurance Div. gave St. Laurent the go-ahead.

The fallout from that decision, however, has garnered considerably more attention—and heated controversy. Last October, just four months after Electric Mutual moved offshore, the company suddenly identified $750 million in potential environmental and asbestos liabilities tied to GE policies. Facing a capital deficit of about $500 million, Electric Mutual filed for liquidation, the equivalent of a bankruptcy filing for an insurance company. The move raises questions about how such a massive hit appeared out of nowhere and questions about GE's role in the debacle. Under Bermuda law, GE, as the sole policyholder of Electric Mutual after the restructuring, can have significant control over the liquidation process. In the U.S., state insurance departments typically oversee liquidations.

GE's advantageous position has reinsurers crying foul. Reinsurers—including Kemper Reinsurance, General Reinsurance, Allstate Insurance, and some underwriters at Lloyd's of London—were paid to provide backup coverage for Electric Mutual's policies with GE. These four reinsurers have filed lawsuits against the Massachusetts Insurance Div., seeking to reverse the move to Bermuda. Their primary worry: that GE will dictate when and how much reinsurers will have to pay on the claims. Those payments go to Electric Mutual, but would eventually flow to the sole creditor, GE. "The concern is that GE will control the show," says Debra A. Hall, general counsel for the Reinsurance Assn. of America. The Massachusetts regulators have asked the court to dismiss the suits, arguing that any harm to reinsurers is speculative.

INSIDERS? Electric Mutual's St. Laurent contends that the reinsurers' contractual obligations and legal defenses do not change simply because the company is in Bermuda. And a GE spokesman says the company did not direct Electric Mutual's restructuring. Still, the deal was handled by an Electric Mutual board elected largely by GE with four of its nine seats held by former GE executives, including St. Laurent, who headed investor communications at the Fairfield (Conn.) giant until 1989. And GE is now poised to take a direct rol



MOVED: *Electric Mutual in Massachusetts*

GE's Offshore Gambit

DEC. 31, 1994 Electric Mutual, an insurer owned largely by General Electric, its biggest policyholder, reports a steep increase in expected payouts on GE policies stemming from environmental and asbestos claims.

JUNE 20, 1995 Electric Mutual applies to Massachusetts insurance regulators to split into two companies. Policies covering the risky liabilities would remain at Electric Mutual, which would move to Bermuda. Less risky liabilities would be transferred to a separate company, Electric Insurance, which would stay in Massachusetts.

JUNE 28, 1995 Massachusetts regulators approve the restructuring. Electric Mutual prepares to move to Bermuda.

OCT. 20, 1995 Electric Mutual identifies $750 million in potential liabilities and files a voluntary petition for liquidation, the insurance equivalent of bankruptcy.

NOV. 30, 1995 Underwriters at Lloyd's of London, who had been paid to provide backup reinsurance coverage for some of Electric Mutual's liabilities, file the first of four lawsuits that seek to reverse the move to Bermuda. Some reinsurers allege that the move will allow GE to exert control over the liquidation process.

APR. 12, 1996 Hearing scheduled for Bermuda authorities to rule on the proposed liquidation.

DATA: COMPANY REPORTS, A.M. BEST CO.

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in the deal: On Dec. 20, the company agreed to pay roughly $125 million to buy the healthy Electric Insurance, which for now is controlled by Electric Mutual through a trust.

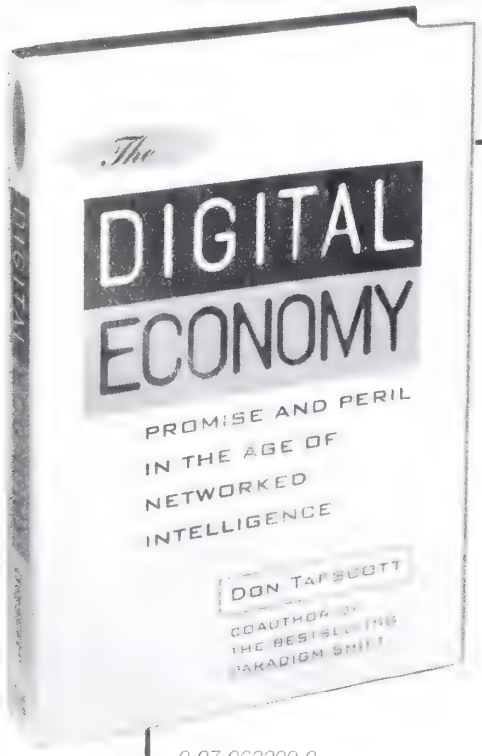
The expected liquidation of Electric Mutual highlights the problems insurers face as the costs of asbestos liabilities and environmental cleanup mount. Standard & Poor's Corp. figures that losses to insurers from claims related to pollution traceable in part to manufacturing by large industrial companies like GE, could top $40 billion—more than 20% of the industry's capital base. And as insurance companies are increasingly forced to pay claims tied to asbestos and environmental problems, they are turning to their reinsurers to cover part of the bill. The collection process can be particularly complicated in insolvencies like Electric Mutual's. "This is the issue for the 1990s," says Hall of the Reinsurance Assn. In the case of Electric Mutual, A. M. Best Co. analyst John H. Snyder figures that the bill to reinsurers for claims could be $100 million or more.

Environmental headaches were of little concern when Electric Mutual was founded in 1927 to provide workers' compensation coverage for GE employees. Over time, though, Electric Mutual expanded, providing multiple lines of business to GE, as well as to outside companies and individuals. Problems began to surface in the early 1990s as the company upped its reserves for future losses on policies in a number of product lines, a move that dragged down earnings. In 1994, Electric Mutual nearly doubled its reserves for asbestos and environmental liabilities, to $185 million. Most of that was tied to exposure to GE environmental liabilities at polluted sites around the country. It was those warning signs that set last year's reorganization in motion.

> Some reinsurers suggest that Electric Mutual relocated to Bermuda so that GE, its largest policyholder, could dictate the terms of the liquidation process

St. Laurent declines to comment on how the new environmental hit sh faced, citing the litigation surrounding the restructuring. But the filing by Electric Mutual for liquidation has raised eyebrows. "You don't just find o overnight that you have a huge env ronmental liability with a big industrial company like GE," says Best's Snyder, who slashed Electric Mutual's rating fr A– to D after the c closure. And Daniel Judson, deputy gen al counsel for t Massachusetts insu ance regulator w signed off on the d said he had fou "nothing in the record to indicate" th Electric Mutual would be liquidat when it moved to Bermuda.

Regardless of the questions su rounding Electric Mutual's collapse seems certain that GE will benefit dealing with the claims in Bermuda stead of Massachusetts. While Electric Mutual executives decline to comme on how the company will be liquidat But in Bermuda, creditors may cho



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an expedited workout, which is not available in Massachusetts. To wind up the process early, Bermuda liquidators can estimate all future claims, generating early payments to policyholders, and therefore early bills to reinsurers for those claims. That means policyholders may collect, and reinsurers may be asked to pay, on claims that haven't materialized yet. In Massachusetts, regulators liquidating an insurance company typically pay claims and bill insurers only as claims are brought. So, while liquidations in the U. S. can take more than 20 years to finish, the Bermuda approach has resolved liquidations in half that time. Unless reinsurers are able to block that process, in short, GE could get its claims money sooner.

"SUBSTANTIAL INFLUENCE." GE could also have a key role in how the insurance tab is calculated. While the state insurance commissioner usually oversees insolvencies in the U. S., in Bermuda creditors generally have a say in appointing the liquidator. So as the only creditor of Electric Mutual, GE may help select and oversee the liquidator. One Bermuda attorney, who declined to be named, says that if GE opts for the speedy resolution, the company will offer evidence of the claims it is likely to be owed in the future. In doing so, GE could help determine how much reinsurers pay on those claims. A General Reinsurance brief said the company "now faces the reality that GE has a substantial and unanticipated influence over the adjudication of GE's own claims."

If so, some reinsurers claim, this would not be the first time. They contend Electric Mutual has in the past cut deals with GE at reinsurers' expense. Electric Mutual filed four lawsuits in 1993 to force several London reinsurers to pay more than $40 million on environmental and asbestos claims the insurer had settled with GE. Attorneys for the reinsurers claim the losses were not covered under the Electric Mutual policies. "It is our position that there was collusion between Electric Mutual and GE," says Alice E. Richmond, an attorney who is representing the reinsurers in the still-pending lawsuits. "They just turned around to [the reinsurers] and said, 'Pay us.'"

GE's ingenious Bermuda gambit could allow it to reap substantial benefits from the liquidation of one of its own entities. But the coziness between Electric Mutual and GE may have a downside. The next time Electric Insurance, the surviving company, needs backup reinsurance coverage, some reinsurers could well run the other way.

By Amy Barrett in Washington, with Tim Smart in New Haven, Conn.

ELECTRONICS

NOT JUST A BLIP ON THE SCREEN

For this mini radar, mass-market potential is huge

You might think that a personal radar system is something you can safely live without. But makers of radically smaller and cheaper Walkman-size radar systems are betting you're wrong. The radar is about to show up in everything from burglar alarms to hand tools. It will measure the water level in toilet tanks and the oil level in car engines. It will warn drivers of blind spots and monitor the triggering of air bags in collisions.

Thomas E. McEwan, a researcher at Lawrence Livermore National Laboratory in Livermore, Calif., stumbled across the concept of personal radar while figuring out how to measure the output of miniature nuclear-fusion reactions created by the lab's Nova laser, the world's most powerful. The technique he devised to monitor the reactions could be used to make a radar receiver, he reasoned. So he put together $10 worth components in a plastic box the size of a pack of cigarettes, and it worked.

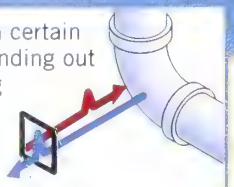
McEwan's "micropower impulse radar" (MIR) sends out about 2 million pulses a second, each lasting at most a few billionths of a second. It works at ranges of 150 feet or less and can run for years on a single battery. It's not only cheap and small but uncannily accurate, capable of measuring distances as small as fractions of an inch. McEwan underestimated its potential at first. "I thought it would make a very cool burglar alarm," he says. "It was the only thing I thought of."

Industry had a few other ideas. In the past two years, more than 3,000 companies have looked into the technology, and 15 have paid $100,000 each to license it. McEwan has 30 patents pending or issued and will probably net about $300,000 as his share of the $1.5 million

RADAR GOES MICRO

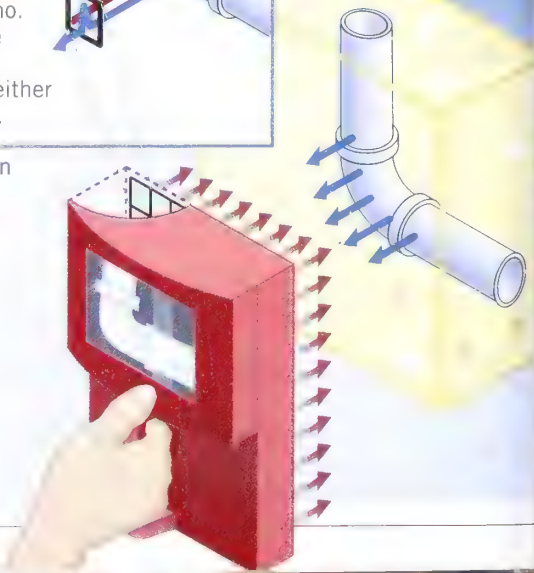
Micropower impulse radar is cheap, tiny, and incredibly accurate at short ranges. Here's how it can locate a pipe in a concrete wall:

1 A radar module "looks" a certain depth into the wall by sending out a short, sharp pulse, waiting a precise amount of time, and watching for an echo. If no echo arrives at the predetermined moment, then the pipe must be either too near or too far away.



2 Each other module in the array does the same, in turn. Then the process is repeated, looking slightly deeper into the wall.

3 A computer collects the data from each pass of the array and processes it into an image of the buried pipe.



oyalties under the terms of Law-e Livermore's patent agreement. won't confirm the figure.)

he first products are coming to mar- Amerigon Inc. of Monrovia, Calif., incorporated McEwan's radar into nsor that helps drivers avoid backing objects. The radar—with warning ts and an audible alarm that rises itch as you get closer—should be l in a half-dozen car models by next ; Amerigon says. The startup also is eloping a complete auto safety sys- with AlliedSignal Inc. Among other ; the radar could tell if a passenger aning forward in the seat. If so, the enger's air bag would open slowly at to ease the passenger back.

E DETECTOR. The most complex mi-ower systems have an array of ra- modules. The arrays can distinguish ges through con- e, under the and, or behind s. A small pro- or combines the a generated by various modules a single image gram). McEwan orking with the ense Dept. on a mine detector and a the Transportation Dept. on a de- to check for corrosion of metal rein- ements in concrete bridges.

ircon Corp., of Campbell, Calif., h makes the popular Stud Sensor, is ing a radar array to spot steel rods oncrete and pipes in walls. It is plan- ; products that can find wires, pipes, sewer lines underground. These s should be more accurate and versa- than the original Stud Sensor, which cts studs inside walls by looking for ations in electrical capacitance. 're going to give the everyday con- tor access to tools that will elimi- a lot of guesswork and frustration," s President John R. Stauss.

IR, like conventional radar, works by ling out a signal and listening for echo. But instead of paying atten- to every echo, it watches only for se coming from a certain distance y—say, 10 feet. The distance is ad- able. That was the key to making system simpler and cheaper. Con- tional radars must sift through and te sense of echoes and stray signals ing from all distances.

IcEwan also came up with an ingeni- way to detect the radar's pulses in- ensively. The system takes a series of apshots" of returning signals, each he precise time an echo is expected k. The snapshots—actually measure- nts of voltage levels—are stored in a acitor and then analyzed using cheap- slower electronics during the lull be- tween snapshots. It may be hard to believe there's much of a lull, with 2 million snapshots per second, but the pulses are so brief that it's proportional to one-second-long pulses separated by gaps of 15 minutes or so.

One early success has been level sensing, the surprisingly tricky business of gauging how much liquid or solid is in a tank. Tanks containing foam, vapor, or dust, as well as tanks with extreme pressures or temperatures, can easily foil even sophisticated sensors. Ultrasound, for example, can be fooled if signals bounce off of thermal layers in gasoline vapors or steam rather than off of the liquid surface. The radar sensor cuts right through to the liquid's surface.

Titan Technologies, which sells level controls for oil, gas, and chemical plants, has introduced an MIR sensor at a cost of $1,000, one-third the price of its mechanical float sensors and about one-tenth the price of level sensors using conventional radar. The price should come down further once the radar and the control circuits it requires are integrated onto a single chip, says John F. Grimes, vice-president at Titan, a Lampman (Sask.) subsidiary of Titan Pacific Resources Ltd. Says Grimes: "Over time, this radar should obsolete all of our products."

VERSATILE Among the first products using the radar is an auto sensor that helps drivers avoid backing into objects

FLASH FLOODS. In the construction field, Cleveland's Pile Dynamics Inc. has built the radar into a system that records how much of a steel or concrete foundation pile remains to be driven into the ground. And for the environment, Remote Data Systems Inc. in Wilmington, N. C., in January introduced a battery-operated surface-water monitor for such uses as watching rivers and streams for flash-flooding or for ensuring that wastewater treatment pools don't overflow.

MIR will really hit the mass market when some company puts McEwan's design on a chip that sells for a dollar or so. McEwan thinks that may happen within a year. Zircon sees a through-the-wall radar priced at less than $50, and Amerigon hopes to sell a car back-up radar that could be installed for under $25. With prices like that, McEwan might find someone willing to build his burglar alarm—a self-adhesive plastic box to be sold on a hardware-store rack.

By Larry Armstrong in Livermore, Calif.

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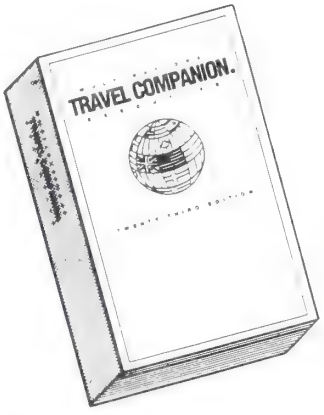

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TED BY PETER COY

PILOTLESS PLANE TO SNOOP OVER BOSNIA

GINNING NEXT MONTH, e skies of Bosnia will be trolled by Predator—an manned surveillance ane equipped with some the U.S. military's most phisticated cameras and dar. An earlier version of edator, whose prime conactor is San Diego-based neral Atomics Aeronautil Systems Inc., began flyg missions in Bosnia last summer. Among other exploits, it confirmed that Serbian guns had not been pulled back from Sarajevo as promised. Now, three Predators have been fitted with an advanced, all-weather radar system from Westinghouse Electric Corp.

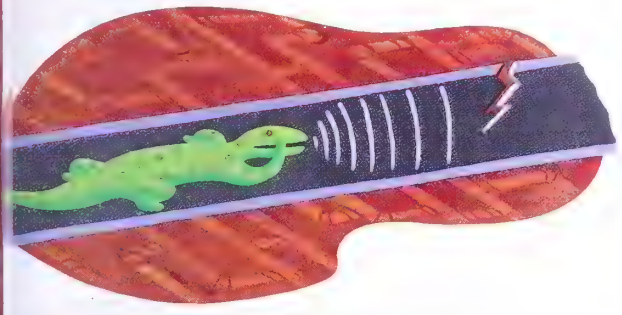
Predator, a 2,000-pound plane with a 48-foot wingspan, can stay aloft for 60 hours. That's almost three days—far longer than manned aircraft. What's more, if the unmanned vehicle gets shot down, "the pilot just turns the key off and goes to lunch, 260 miles away," says Thomas J. Cassidy Jr., president of General Atomics Aeronautical. Predator costs less than $4 million, or a tenth the price of a military recon jet. Out of the line of fire, Cassidy says, Predator could be used for monitoring oil spills, forest fires, river traffic, and national borders.

ECKING ELINES WITH ALAMANDER

LINE COMPANIES USE SOd intelligent pigs to travrough pipes and look for age. The mechanical sys- are good at finding wallning corrosion but can't detect small cracks. To find those, inspectors fill a pipe with water and jack up the pressure to see if it springs a leak—not an ideal solution.

Pipetronix in Karlsruhe, Germany, says it has an answer with a new addition to the pipeline zoo: the Rissprüfmolch, or "crack-inspecting salamander." It spots cracks using 896 transducers that send out overlapping waves of ultrasound. The sheer number of transducers provides the salamander with ultrakeen vision. It can detect cracks as short as a centimeter, even if the walls of the crack are pressed together.

The ultrasonic salamander—developed with Germany's Fraunhofer research centers—is battery-powered. It is pushed along by fluid flowing through pipes up to 56 inches wide. Because it may have to travel hundreds of miles before coming up for air, it can record hundreds of gigabytes of inspection data on digital tape. No petting or purchasing allowed: It's only for Pipetronix' own inspectors.



AN THIS TEST AVERT SUICIDES?

PRESSION CLAIMS MANY VICTIMS, BUT ly a fraction of them are actually at risk suicide. The problem is figuring out ich ones. Psychiatrists administer questnnaires and other behavioral tests, but at's an inexact science. Now, researchers the University of Illinois' College of edicine in Chicago have devised what ay be a tipoff test—a way to spot signs suicidal tendencies in a patient's blood. Scientists discovered years ago that the ains of suicide victims reveal high levels a protein called 5-HT2a. This didn't help ctors at the bedside, though, because it's impossible to measure the level of 5-HT2a in the brain of a living person. Now a team led by pharmacologist Ghanshyam N. Pandery has found high levels of 5-HT2a somewhere else: in the platelets of 43 people who had attempted suicide. Because platelets circulate in the bloodstream, they can be easily inspected for the telltale protein.

Pandery says he isn't sure why elevated levels of 5-HT2a should appear in the platelets of potential suicide victims. But whatever the cause, if the new test proves an effective marker in larger studies, it could become a powerful tool to prevent suicide.

INNOVATIONS

■ The hemoglobin in red blood cells is the inspiration behind a new kind of molecular computer memory proposed by a multi-university team headed by scientists at the University of Southern California. Hemoglobin functions by picking up and releasing an oxygen atom—a good model for storing bits of data in tiny computers, notes USC chemist Larry Dalton.

■ Chairsores might be a better term for the bedsores that afflict thousands of people who are forced to sit motionless in wheelchairs. So university scientists in New Mexico and California have designed an "active" seat cushion. It won't let people sit still. If its sensors don't detect movement for a while, the cushion forces the patient to change position by pumping air from one place to another. It will be marketed by Numotech in Sun Valley, Calif.

■ W.J. Sunns Inc. of Englewood, N.J., has developed the Smart Valve, a leak detector that knows if a faucet is dripping or if a pipe has burst. The $500 Smart Valve can sound an alarm or even shut off the water at the meter, says Sunns President Josef Wodeslavsky, its inventor.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwfeb@businessweek.com

TELECOMMUNICATIONS

MCI IS SWARMING OVER THE HORIZON

Its deregulation plan: Offer all the consumer services it can

Well, it's finally here. After years of dickering, Congress passed a landmark bill on Feb. 1 that deregulates every aspect of the communications business, allowing cable-TV providers, local phone companies, and long-distance carriers into one another's markets for the first time. It brings to a logical conclusion the process started by MCI Communications Corp., the company that in 1968 became the first to challenge the Bell System in long distance. Since then, MCI has built a reputation as a marketer par excellence, clawing 20% of the nation's long-distance calls away from AT&T.

Based on its history, MCI would seem to be an odds-on favorite in the competitive free-for-all that is about to engulf the telecom industry. But in the much more broadly defined communications market that's coming, MCI has to learn how to sell a lot more than long distance to survive. "It's no longer a question of how large a share of the $75 billion long-distance market you can get," says UBS Securities Inc. analyst Linda B. Meltzer. "It's a question of how big a share of the $500 billion converged or integrated market they will get."

ON AND OFF. Until recently, MCI has been vexingly vague about how it plans to do that. Starting and then stopping two different wireless strategies and an online service effort didn't help. But thanks to a recent flurry of deals, culminating with a Microsoft Corp. online partnership and a direct broadcast satellite (DBS) venture with News Corp. in late January, MCI has finally pulled together a cohesive convergence strategy. Now comes the task of getting all those pieces to work together. MCI, the only purely long-distance carrier, still has something to prove on that score.

Its plan: Concentrate on selling services, as many as possible. Through joint ventures, partnerships, resale agreements, and new MCI initiatives, the company will offer just about any service that comes over a wired or wireless communications system, including satellite TV, Internet connections, electronic commerce transactions, and of course, local, long-distance, and international phone calls (table). "We want to get as many hooks into each of our customers as possible," says MCI Chairman and CEO Bert C. Roberts Jr. MCI studies show that customers who buy more than one service switch carriers at a 40% lower rate.

This, of course, is the same mantra that all the phone companies are reciting: Offer a single source for long-distance and local calling, video, data, and wireless services, bundle them onto one bill, and customers will come (page 32). That's the driving force behind the flood of alliances, acquisitions, and restructurings in the telecom industry. No one can afford to stay in one telecom sector anymore. The new telecom law breaks open the cozy oligopoly of the big three long-distance carriers, which control 90% of the long-distance business. In 18 months or so, the seven Baby Bells and GTE Corp. will enter the market, putting downward pressure on prices and upward pressure on marketing costs. And any local calling business that MCI, AT&T, or Sprint gain will carry a much lower profit margin than long distan "The current environment for long d tance is relatively benign," says J. P. M gan Co. analyst Simon P. Flanne "There are no marketing wars right n no real pricing pressures, and acc charges continue to come down. It's dream world, and it's about to end."

MCI insists that its long history a scrappy upstart and savvy marketi machine will give it the edge in t harsher world. Indeed, the cocky co dence of its top executives is legenda But various studies indicate that the lo phone companies could grab as much 10% to 15% of the long-distance mar in their home regions. An executive a local carrier warns: "If MCI thinks th are the only ones who know how to m ket, they are due for a fall. They sho recognize that."

Roberts does recognize the need diversify and says he wants MCI to p in 50% of its revenues from new ve tures by 2000. The company has spe more than $6 billion over the past ye buying everything from a cellular-pho reseller to SHL Systemhouse, a Ca

FLEXIBLE
Have some moves been contradictory? CEO Roberts says: "We are quick to move forward and quick to pull back when we have to"

-based computer systems integra- And it has built fiber links in 25 ; to provide local service to business)mers.

iese new ventures, though, won't ; producing profits for some five s. MCI just reported a 20% gain in earnings, to $1.07 billion—before ucturing charges—on a 14% gain in nues, to $15.3 billion. But 1996 will)ugher, say analysts. J.P. Morgan's nery estimates that MCI's new ven- ; could dilute earnings by more than a share in 1996. "They will be survi- but I'm not sure they can continue eport double-digit earnings growth e next few years," he says.

ill, MCI keeps plowing ahead—though hat one executive concedes could be as a scattershot approach. Last for example, MCI spent $2 billion 13.5% stake in News Corp., an in- ment that left industry observers :ching their heads over the seeming of synergy. The arrangement be- e clearer on Jan. 25, when MCI and s Corp. announced a joint venture to d $1.3 billion building a DBS net- ;. But three days later, Roberts an- iced a broad alliance with Microsoft makes MCI the primary distributor of Microsoft's online network. Only problem is that for the past five months, MCI had been an equal partner in an online network with News Corp. "We are pushing our boat in Microsoft's waters," Roberts said.

Its wireless strategy has also been erratic. In February, 1994, it bought a stake in wireless startup Nextel Communications Inc., then bailed out eight months later. It talked to a few of the Baby Bells about bidding jointly for licenses for the new wireless Personal Communications Service (PCS), but could not reach an agreement. Instead, MCI plans to resell wireless service purchased from others, figuring that once PCS networks are built, there will be a glut of capacity. To beef up its wireless marketing, MCI paid $190 million last September for Nationwide Cellular Services Inc., a large reseller.

MCI is honing its reselling skills with paging. It started offering paging services purchased from two suppliers in May, slapping on its brand and providing billing, service, and sales. MCI already has more than 500,000 customers.

Analysts say MCI could be just as successful in the cellular calling business—if there is a capacity glut, though that isn't a given. "Building your own network is incredibly capital-intensive, so they'll save a lot of money," says Mark Lowenstein, consultant with market researcher Yankee Group Inc. "But the profit picture is quite a bit muddier. They'll be trying to negotiate rates with the same companies they compete against."

MCI's changes in direction may strike some as erratic, but to Roberts, they are evidence of MCI's flexibility—and its strength. "We're quick to move forward and quick to pull back when we have to," he says. And many analysts say it doesn't really matter how many times MCI switches direction, just where it ends up. "This industry is moving at gigabit speed," says Bear, Stearns & Co. analyst William N. Deatherage. "I think midcourse corrections in your strategy are unavoidable." MCI's recent moves have finally put some life into a stock that substantially underperformed the market last year. Shares rose from 26 in early January to 29¼ on Jan. 29, after the Microsoft and DBS deals were announced.

SHARING RISK. MCI also says its strategy is based on a consistent set of principles. "We buy when there are finite resources and lease when there is a glut," says Timothy F. Price, president of MCI's long-distance business. That's why MCI was willing to pay $682.5 million for a slot for its DBS satellite, twice what analysts estimated it should cost: It was the last one available. But it's a high-risk strategy, given that DirecTV has a two-year headstart and has just taken on a powerful partner—AT&T. "I felt good about the [DirecTV] deal when I made it," says Joseph P. Naccio, head of AT&T's consumer business. "I felt a lot better after I saw the price MCI paid for those licenses."

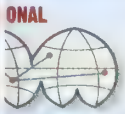
MCI will at least share the cost of its DBS venture—another strategic tenet. Roberts wants to take on partners as often as possible in order to spread around the risk, be it with Murdoch, Gates, or British Telecommunications PLC, which bought a 20% stake in MCI in 1994. "I'm not so visionary that I know where all the bucks are going to flow five years from now," he says.

Besides, argues MCI, vision is not as important as killer marketing instincts. "We don't want to dive in ahead of where the customer is," says Price. He just wants to move as fast as possible to where they are. MCI's speed has impressed Peter Bonfield, British Telecom's new president. "They're bloody fast. They can turn an idea into a product in a month." Now, Roberts just needs to hope that it takes the local phone companies longer to figure out the long-distance market than it takes MCI to figure out its new businesses.

By Catherine Arnst in Washington

MCI's Future Comes Into Focus

With deregulation looming, phone companies are getting) offer bundles of services—by developing new lines of business or by 'iking partnerships with other companies. MCI, which still gets f its $15 billion revenue from long distance, is less diversified than long-distance rivals AT&T and Sprint. But it has a lot of new businesses cooking.

	DESCRIPTION	1995 REVENUE
	MCI Metro is building fiber-optic loops in major cities to connect businesses directly to its long-distance network	$108 million
DATA HG MAIN MENU	After striking a deal with News Corp. for half interest in an online venture last fall, on Jan. 30 MCI backed off and announced a sweeping new deal with Microsoft	None
	MCI and News Corp. plan to spend $1.3 billion over the next two years developing a direct broadcast satellite network	None
ONAL 	Joint ventures include Concert, a partnership with British Telecom to offer global networking services to major corporations, and Avantel, a Mexican long-distance venture with Grupo Banamex-Accival	$228 million
E NETWORKS	Through its $1 billion purchase of SHL Systemhouse, MCI is now in the business of handling corporate telecom networks	$135 million
	With no network of its own, MCI is reselling cellular service and bought Nationwide Cellular, a national reseller	$93 million

DATA: COMPANY REPORTS

REVOLUTION IN

Finally, consumers are in the driver's seat–and pushy dealers look like dinosaurs

That sick feeling began as soon as Joan Bondio drove her new Honda Accord off the lot a month ago. Did she pay too much? Did she get enough for her trade-in? Like a lot of other car buyers, Bondio, 47, found the Darwinian car-buying process intimidating and traumatic. "The feeling that you got taken bothers you," says the Parma (Ohio) bank executive assistant. "I'd never bought a car before, and I was afraid."

That's about to change. The dreaded auto showroom, with its gilded illusion and sweaty-palmed reality, is fast becoming an endangered piece of Americana. The tradition of smarmy salesmen, high-pressure tactics, and arbitrary pricing continued unchanged for decades following World War II. But now, the forces that have lately revolutionized the rest of retailing are about to transform the way we buy cars.

Cover Story

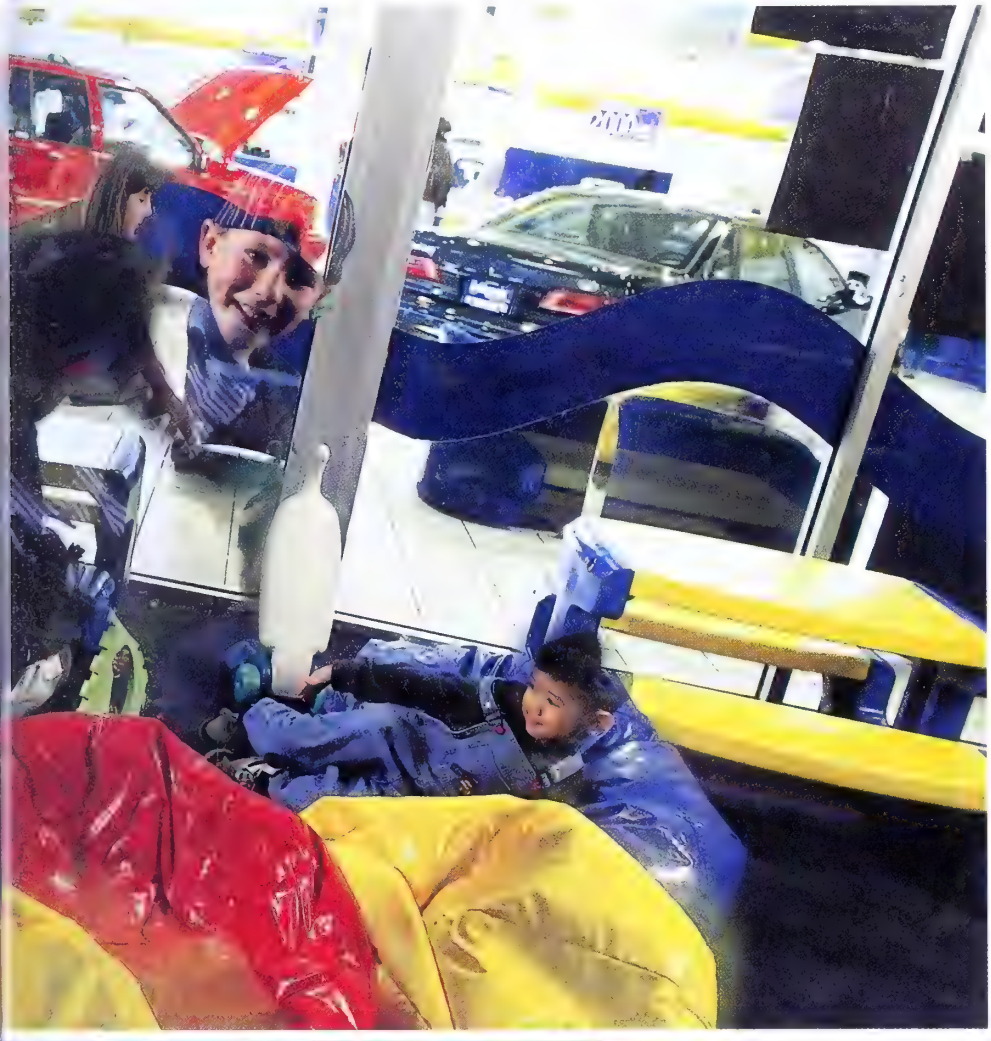
Signs of that transformation are everywhere. Car shoppers are logging on to Internet buying services to peruse specifications and check prices. They're dialing up auto brokers who will handle the dirty work of negotiating for them. They're ogling the wheels at warehouse clubs, which have used the buying power of their vast customer bases to build networks of dealers willing to give cut-rate prices. They're visiting giant auto malls carrying several different lines of car, where they can—gasp!—comparison-shop. And they're bargain-shopping at used-car superstores that offer vast selection and no-haggle pricing (table). "There is no longer one way to buy a car," says J. Ferron of Coopers & Lybrand Consulting. "The consumer is making the rules."

These newfangled distribution channels are already enjoying explosive growth. CarMax, the used-car chain that electronics giant Circuit City Stores Inc. is rolling out nationwide, did an estimated $288 million in sales at just four stores last year. In 10 months on the Internet, AutoByTel helped broker more than 25,000 car purchases last year and is bracing for a fivefold increase this year. More than a half-million car shoppers have turned to Sam's Club, Wal-Mart Stores Inc.'s warehouse

Driving Car Sales in a New Direction

COMPANIES	CONCEPT
CARMAX (Circuit City), **AUTONATION, CARCHOICE**	Used-car superstores; CarMax has one Chrysler new-car fran… CarChoice offers child care and a café.
SAM'S CLUB (Wal-Mart), **PRICECOSTCO**	Telephone-based referral services to dealer networks that pro… bargain prices for club members.
AUTOVANTAGE (CUC Int'l.), **AUTOBYTEL, CONSUMERS CAR CLUB**	Telephone/online-based brokers who negotiate low, no-haggle… AutoVantage offers access to specs, options, and dealer cost…
CENTURY 21	Discounts on GM cars for employees, franchisees, and custon…
UNITED AUTO GROUP	Partnership headed by former adman Carl Spielvogel has bou… 41 dealerships. Offers efficiency and better customer service…

HE SHOWROOM



SHARP TURN

Child care at a CarMax in Atlanta (above); computer kiosks at a prototype Chrysler dealership in Dallas (left)

club, since 1991 for referrals to its dealer network. The numbers are still small in a $605 billion market where 45 million new and used cars change hands annually. But a sea change is under way, says respected automotive trend watcher J. D. Power & Associates Inc. "A powerful new force is being unleashed," says Power's Don Keithley. "People are realizing there are new choices available, and they are not going to want to buy cars the same way again."

STREET GANG. Protected by strong franchise laws, the creaky, antiquated, and inefficient dealership system is where general-merchandise retailing was 30 years ago. But now, some big and smart money is betting that the auto showroom is finally ripe for change. Circuit City, which grew to a national powerhouse selling TVs and computers, is applying its formula to high-quality used cars. H. Wayne Huizenga, the former Blockbuster Entertainment Corp. chairman, plans to do for cars what he did for videos with a competing chain, AutoNation. Wall Street sees opportunity here, too: Financial heavyweights, including New York financier Marshall S. Cogan, Leon D. Black of Apollo Advisors, and J. P. Morgan Capital, are major investors in United Auto Group, the nation's fourth-largest new-car chain.

No one will be happier to see change than the car-buying public, which finds purchasing an automobile "the most anxiety-provoking and least satisfying of any retail experience," according to a recent survey by Yankelovich Partners Inc. "It's a game," said Rene Rouillard, a 42-year-old carpenter in Westfield, Mass., as he shopped recently for a new van for his business. "They know the rules, but you don't."

But consumers have gotten a taste of something better. The advent of superstores, shopping malls, and upscale department

Someday soon, new cars may be sold in auto supermar

stores has made shopping for just about everything other than cars faster and easier than ever. The rise of giant retail chains has forced manufacturers to bring down the prices of everything from tools to televisions. Now, consumers are demanding the same selection, service, and rock-bottom prices when they buy their wheels.

The new players bring a new kind of retailing savvy to car sales. They see cars as fundamentally the same as shoes or TV sets, products that sell best with the right blend of selection, convenience, service, and price. Their methods foreshadow a time when cars will be sold in automotive supermarkets where competing brands will sit side by side like so many cans of soup.

Cover Story

It's a revolution Detroit views with mixed emotions. Carmakers would like dealers to improve the showroom experience. After all, they spend hundreds of millions of marketing dollars to turn their products into exalted objects of desire. And they spend hundreds of millions more to persuade consumers to step into the showroom—only to have them abused and alienated. Yet the fragmented networks of small, family-run dealers give carmakers a measure of control—control they won't have over giant retailers selling multiple brands at multiple outlets. No longer will Detroit be able to impose its choices on the marketplace, knowing dealers will strong-arm shoppers into buying whatever carmakers send them. "The world is changing," says Chrysler Corp. Chairman Robert Eaton. "We don't know where it's going to go, but we know it's going to change."

HIGH COSTS. Already, the new players are offering relief to beleaguered car buyers. Used-car superstore chains are filled with the customer-friendly amenities such as child-care centers, coffee bars, and touch-screen computers that shoppers have gotten used to in the likes of Nordstrom Inc. department stores, Ikea furniture stores, and Barnes & Noble bookstores. Salespeople on salary instead of commission provide assistance and advice rather than a high-pressure assault. The new gadgets allow shoppers to browse a huge inventory of cars marked with low, no-haggle prices. As Kelly Wilson shopped for a pickup at the new CarChoice used-car hypermarket near Dallas, her daughter played in the store's child-care center, watched by a CarChoice nanny. "Anyone with children will like this," says the 23-year-old graphic artist. "It's difficult to shop wi kid whining to go home."

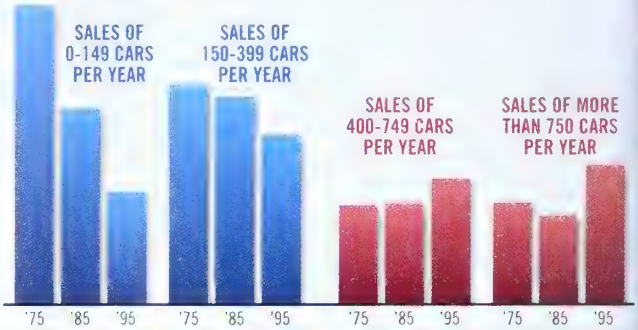
Vast rows of gleaming cars, banks of computers, and pr real estate are beyond the means of most family-owned d erships. Those small operators just won't have the finar horsepower to match CarMax, AutoNation, and the ot used-car superstore, CarChoice, backed by shopping-mall veloper Waad J. Nadhir. Analysts estimate their mass stores cost $20 million to build, dwarfing the $4 millio takes to set up the average new-car dealership. "It's getting capital-intensive to remain a private family-owned busine says Michael Lazarus, a Long Island (N.Y.) Saturn de whose grandfather got into the trade in 1926 by buy Brown's Auto Auction in Manhattan—then located across fi a horse auction. Lazarus is afraid his sons, who will one take over the business, won't be able to remain independe

If they decide to cash out, they can turn to a new breed dealer—Wall Street investors who are amassing portfolio large dealerships. That's accelerating a long slide in the nu ber of dealerships, which has slipped from 47,500 in 195 22,400 today (chart). And it won't end soon. At the Natio Automobile Dealers Assn. (NADA) convention under way month in Las Vegas, legendary adman Carl Spielvogel, CE United Auto, is "booked solid" meeting with dealers looking sell. Spielvogel says his company was founded four years on the premise that it can "revolutionize cars the way W Mart and Home Depot did to retail." In an industry that tended to keep bankers' hours, his stores are open from 8 a to midnight and feature full-service cafeterias, playgrounds, spiffed-up waiting rooms. United Auto sells 22 brands, fi

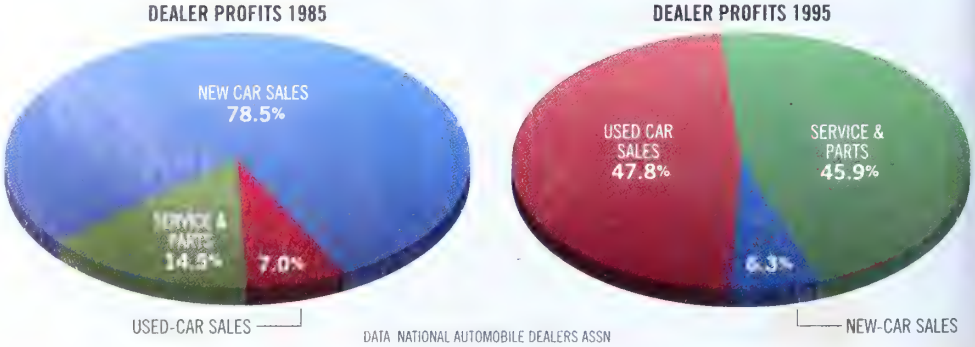
Signs of Consolidation

THE RANKS ARE THINNING...

...ONLY THE LARGEST DEALERSHIPS ARE GAINING...



...AND DEALERS AREN'T MAKING MUCH MONEY SELLING NEW CARS ANYMORE



DATA NATIONAL AUTOMOBILE DEALERS ASSN

l with competing brands

ɔs to BMWs. Business is booming at the fast-growing 41-chise chain, and Spielvogel says he may take it public. hat possibility, more than anything else, may pose the est threat to the status quo. With his limited resources, the pendent dealer has been locked in an uneasy standoff ı Detroit. A national chain able to sell shares to the public d achieve the kind of clout that has allowed Wal-Mart to ate terms to its suppliers and to obtain huge advantages its smaller competitors.

T'S THE DEAL? Not all dealers are heading for the exits. e of the largest U.S. dealers fired back at the big-money ers on Feb. 7 by launching Driver's Mart, a chain of used-superstores that plans 100 outlets across the country in five s. "With outside organizations that have access to capital kets invading our industry, we must e to combine our resources," warns ald E. Flow, a Winston-Salem (N.C.) adealer and Driver's Mart's chairman. dealers hired a retailing expert, for-Amway Corp. executive Thomas W. leston, to be CEO, and they lured au-ɔtive quality guru J.D. Power III to n their board. Flow says the dealers considering taking Driver's Mart pub-nd industry sources say a major auto ɔany could take an equity position.

he new superstore chains are so far entrating on used cars, where they have to wrestle with restrictive state chise laws. But that doesn't comfort -car dealers, who depend on used cars alf of their earnings, with service and s making up most of the rest (chart). hroat pricing practices and rising over-have sliced profits on new cars to st nothing. And with a rich supply of -quality, late-model used cars—thanks to the growing pop-ty of two- and three-year leases—and new-car prices that age $20,000, more consumers are opting for used cars.

ıe looming battle is over shoppers such as Cynthia Chance, vho swore off traditional car buying after she discovered Max last year. Chance, who once had a new-car salesman t at her to call her father for help when she balked at ng a deal, says she always hated the process. "To get the deal, I had to act like somebody I wouldn't have gone to ı with," says the ethics instructor at Mount St. Mary's Col-in Emmitsburg, Md. Chance bought a Honda Accord at Max last year and closed the deal on a Sunday.

ıyers such as Chance have forced Detroit to take notice. rsler stunned its dealers and competitors last month by ıg CarMax a new-car franchise in Duluth, Ga. Chrysler it a test, but the move has infuriated dealers. "Chrysler ɔpened a Pandora's box, and they'd better snap the lid on very quickly," says Jim Muir, a Sterling Heights ı.) dealer. General Motors Corp.'s dealers are even more aged. GM's marketing chief, Ronald L. Zarrella, has ched a $1 billion crusade to eliminate 1,500 of its 8,500 ers over five years, as GM wrestles to bring its bloated l network in line with its diminished market share. it any wonder that a new J.D. Power survey finds ers are pessimistic about their future for the first time 1989, back when a recession was brewing? "What we're ıg in the auto business is parallel to what's happened her areas of retailing," says consultant John Bissell underson Partners in Bloomfield Hills, Mich. "Mass

CYBERDEALERS

High Technology, Low Aggravation

Jim and Lisbeth Echeandia, co-owners of a candy-industry trade magazine, like a sweet deal, but they don't much like fighting for it. That makes car buying a turnoff, an ordeal Jim usually prepares for "like a heavyweight fighter preparing for a major bout." But their most recent purchase was more like a cakewalk. The Plano (Tex.) couple bought a $30,000 1996 Jeep Grand Cherokee Laredo with a V8 engine last month in just 45 haggle-free minutes.

Lured by a newspaper ad, the pair drove 20 miles to Dallas' MidPark Jeep-Eagle Inc., where Chrysler Corp. is testing a high-tech, low-hassle dealership. The emphasis is on speed and service. Computer ter-

SHORT AND SWEET: *The Echeandias took less than an hour to buy a Jeep*

minals gave the couple quick access to information to make comparison shopping easy. A no-haggle policy means the sale price is the same for everyone.

The Echeandias, Jeep loyalists who wanted to replace Lisbeth's '89 Cherokee, had visited two other dealers but weren't happy. At MidPark, they found a vehicle with the features they wanted plus a few extras they hadn't planned on, negotiated a trade-in on the old car, and closed the deal in about the time it takes to have lunch. A single salesperson handled the whole transaction. The price? About $1,000 below the lowest price other dealers wanted. More important, says Jim, was the new way of doing business. "I don't like negotiations," he said. "Here, I got the best deal, and nobody is going to get a better one because he has a better tongue. This is a long overdue change in auto retailing."

When it's time for a tune-up, a "smart card" will let them access an ATM-like machine to drop off and retrieve keys to the Jeep 24 hours a day. If Lisbeth decides to wait while the oil is changed, she can plug a laptop into a MidPark workstation. "It's like going to the Admiral's Club between flights," she says. That should make the hassles of car ownership a little easier to swallow.

By Jeff Hoffman in Dallas

STEVEN PUMPHREY

Detroit doesn't mind friendlier dealers, but it's wary o

merchandisers are in. The middleman is disappearing."

In the automotive supermarket envisioned by industry futurists, Ford Escorts would share shelf space with Toyota Corollas and Dodge Neons. Customers would browse the aisles, make their selections, and simply pay the price tag.

Not so fast, say dealers, who are protected by some of the strongest franchise laws on the books. Dealers provide 20% of sales taxes in many states—not to mention a hefty share of local TV and newspaper advertising—and they've used their political clout to enact dealer franchise laws that have made it hard for national retailers to enter the new-car business or for Detroit to control the pricing and promotion of its own products.

Cover Story

There's one common denominator in the crazy quilt of widely varying state franchise laws: Newcomers are effectively shut out of the new-car business by laws that prevent auto companies from issuing a new franchise within, say, 15 miles of another dealer. In order to grant or revoke a franchise, carmakers must go before dealer-friendly state motor vehicle boards. The net result: Dealers have more say than manu turers over who is let in and out of their exclusive club.

"The sea change in retailing has happened all around dealers because they've been protected by some of the m anticonsumer and anticompetitive laws in the nation," s Thomas Kinnear, professor of marketing at the University Michigan. But J. D. Power predicts that within 10 ye auto manufacturers will begin circumventing the traditio franchise system by opening factory sales outlets and est lishing new channels of distribution through national retail like Sears, Roebuck & Co. or Wal-Mart.

"ENORMOUS COST." The franchise laws also create inefficie and unnecessary expense. The traditional dealership syst with different stores for each brand, "adds an enormous cost the distribution system," says Circuit City Senior Vice-Pr dent W. Austin Ligon, who oversees CarMax. "Imagine wha would cost to buy a TV if Circuit City had to have 15 differ stores to sell 15 brands of television," says Ligon.

Like the mom-and-pop hardware stores and bookstores fore them, the independent dealers claim they bring a leve loyalty and stick-to-itiveness a big corporation can't mat

ONLINE SERVICES

Info Highway to Heaven

Lonnie Reeder, 39, hadn't bought a car since 1987, when it took close to four tense hours just to hammer out the price. But her recent experience was vastly different. This time, the salesman was expecting Reeder and her husband, Frank, and the price was already set. "It was a done deal within a half an hour, and we figure we saved several thousand dollars," says Reeder, a freelance video producer in San Jose, Calif.

CONVENIENCE: *An online broker helped Reeder make a deal*

Reeder's secret? CUC International's AutoVantage. CUC, the Stamford (Conn.) membership service that hooks consumers up with discounted prices on everything from refrigerators to VCRs, started its auto service in 1988. Members pay $49 a year for access to reports on everything from car features to safety. Once they make a decision, they dial CUC's toll-free number. CUC gives them a firm price for the model and options they want from one of the 2,000 dealers in its network. They can buy from that dealer or use the quote to negotiate elsewhere.

AutoVantage also has online areas in the major services, such as America Online, where members can log on for information on features, safety and repair records, and the dealer's invoice price. That's where Reeder found AutoVantage. "Convenience was a big issue," she says. "Being able to log on and just browse to my heart's content was great." Reeder also called CUC's customer representatives regularly with questions before deciding on a Honda Civic.

First, though, she and her husband went to a local Honda dealer who wasn't affiliated with AutoVantage to take a test drive. They knew a lot about the car but didn't yet have a CUC price quote. Reeder and her husband tried bargaining, but the hard-selling dealer wouldn't budge: He wanted $18,000, without tax and licenses. Reeder says negotiations were tense. "It almost came to a name-calling situation," she says.

The next day, she called AutoVantage and got a referral to a network dealer for the same model with the same options. The total price, including tax and license, for her turquoise Honda? About $16,000. Reeder says her husband will be in the market for a new car later this year. Don't expect to see him roaming the showrooms.

By Lori Bongiorno in New York

t big chains might wield

e manufacturers want somebody with their own money in-
ed in that store," says Frank E. McCarthy, NADA's execu-
vice-president. "That's the guy who is going to work the
hours to make it profitable."

ut there's an eerie sense of déjà vu to McCarthy's words.
l-Mart had the same image as CarMax when they first
e in, and all the local retailers said they wouldn't be wiped
because they knew the market better," says Robert Blatt-
g, a retailing professor at Northwestern University. "But
-Mart ultimately won." Indeed, the national chains already
n to be proving they know more about satisfying the cus-
er. CarMax enjoys an amazing 98% cus-
er satisfaction rating, while NADA says its
lers satisfy 85% of their customers and
r surveys put it as low as 65%.

lot that the auto companies are just idling
r engines while outsiders redefine their
iness. The Japanese auto makers' luxury
sions, Lexus and Infiniti, helped establish
levels of customer pampering and show-
n style. Chrysler and others distribute
luct information from computer kiosks in
pping malls and convention centers. Saturn
rying to remain in the forefront with
tibrand used-car departments that offer
same no-haggle pricing and 30-day ex-
nge policy as its new-car departments.
l Ford Motor Co. and GM continue to ex-
iment with a variety of one-price concepts.
Auto makers can only suggest. It's up to
r dealers to implement innovations such as
er customer service and low-pressure, no-
gle pricing. Of 1,200 rival dealers who attempted to imitate
urn's no-dicker stickers, only 400 have stayed with it. The
found the practice couldn't last in a market oversaturated
h dealers who survive by undercutting their neighbor.

FEE SHOP? But the carmakers can't allow dealers to stay in
ruts. Chrysler is experimenting with a dealership-of-the-
ure concept dubbed Modus after the custom software system
uilt to go with it. The company is trying the idea at an in-
endently owned Dallas Jeep-Eagle dealership, outfitting it
h so much high-tech gadgetry that the computers appear to
number the cars in the showroom. Shoppers can check
del offerings on touch-screen kiosks or use computers to
ck out a database of competing models. Free gourmet cof-
and play areas for kids help them feel at home.

Chrysler hopes to persuade its dealers to take the concept
ional. But dealers wonder how they will afford all these fan-
features when their overhead costs already eat up most of
ir new-car profits. "My customers are not going to give me
00 more because of a sandbox for the kids and a computer
the floor," scoffs Martin J. "Hoot" McInerney, 67, a South-
d (Mich.) megadealer.

But many shoppers don't want to set foot in a showroom, no
tter how good the cappuccino. Tens of thousands are flock-
to the Internet or auto-buying clubs. Ken Ross, a software
pany CEO in San Francisco, recently bought a BMW 530i
ough Consumers Car Club, an auto broker. Ross, 53, had al-
dy gone a few rounds with a "typical car salesman" at a
W dealership. The broker, whom Ross only spoke to by
ne, went to a different BMW dealer and managed to nego-
e a price of $37,500, $5,500 off the sticker. All Ross had to
was pick up his car and sign the paperwork. "I hate nego-
ing," says Ross, who paid a $50 fee to the broker. "You go
ough all that hassle, and then your buddy tells you he got

SUPERSTORES

Buying Used–Without Feeling Used

Hiram Colon knows better than to try to beat a car salesman at his own game. After all, the 48-year-old Stone Mountain (Ga.) resident used to sell Toyotas. He knows all about enticing customers with a low base price and then loading on expensive options, or tacking on costly warranties and service contracts. "There's no such thing as beating a car salesman," says the real estate seller.

So when his wife, Grace, recently said she wanted a 1996 Toyota Camry, he reluctantly started to comparison-shop at local dealers, warning the sales staff that he knew the inside scoop. "They still tried to give me the runaround," he says. That's when he decided to visit the CarMax used-car superstore in Duluth, Ga. He called ahead and requested a Spanish-speaking salesman, who turned out to be more like a clerk in a department store than a traditional car salesman, Colon says. Since there's no haggling over CarMax prices and commissions are based on unit volume and not price, the main job of the sales staff is to answer questions and smooth the process rather than steer customers to higher-priced models.

"NO PRESSURE": *Grace and Hiram Colon with their '96 Camry*

Using one of the CarMax computer kiosks that dot the showroom floor, Colon punched in the amount of his downpayment, the monthly payment he thought he could afford, and the model and options he was looking for. The computer spit out a picture of a shiny gold 1996 Camry, with 7,400 miles and a sticker price of $18,900. After a quick test-drive, he and his salesclerk finished a loan application. Based on his income, credit rating, and a $2,000 downpayment, CarMax financed the rest at 16%. Colon says he was pleased with the price, and since CarMax doesn't tack on any prepayment fees, he plans to refinance the loan in six months through his bank. The whole process took about two hours, and as Colon marvels: "There was no pressure. I was very relaxed, and I felt like I was in control." That's not a feeling most car buyers get to experience.

By Nicole Harris in Atlanta

ANN STATES/SABA

his car for $100 less." Consumers Car Club, which logs 500 inquiries a day and negotiated $250 million worth of car sales last year, is taking its brokerage onto the Internet on Apr. 1.

It won't be alone. A growing number of dealers and brokers are taking to the Info Highway. AutoByTel has been brokering deals from its site on the World Wide Web since last March. It runs a free referral service with a network of 1,400 dealers, who pay $500 to $3,000 a month and agree to sell at low, prenegotiated prices. CUC International's AutoVantage service, available through online services or by phone, has attracted about 2 million members who pay $49 a year for access to its database of specs and prices. Last year, it negotiated more than 10,000 car sales and expects to almost double that in 1996.

"IT WAS FUN." Not to be outdone, some dealers and manufacturers are taking the wheel themselves on the Internet. On Feb. 5, GM launched the world's largest automotive Web site with links to each of its divisions, encompassing more than 16,000 pages of information. Meanwhile, more than 125 dealers have linked up with DealerNet, a World Wide Web site that offers competitive specs and approximate prices on cars but does not broker transactions. Even software giant Microsoft Corp. has taken a spin at providing auto services on the Web with CarSource, which offers facts and figures about most models on the market.

Car buyers who surf the Net first find they are well-armed when they hit the showroom. Alice Hill, an editor at an online magazine in San Francisco, pulled dealer invoice prices off CompuServe Inc.'s Auto Net before she started shopping for a Honda Del Sol last year. Her salesman wanted to start the bargaining at the car's $24,000 sticker price, but Hill countered by citing the invoice price of under $13,000. The salesman's "face just dropped," says Hill, who eventually bought the car for $14,000. "It was fun. I can't wait to buy another car."

Not all buying services are high-tech. Wal-Mart is dabbling in the car business. Shiny new cars are on display at some of its Sam's Club warehouse clubs. Shoppers can look at the sheet metal, but they must head to the dealer for a test drive and to close the deal. The dealers in Sam's referral network are supposed to offer club members a bargain price. Michael Mullaney went to Sam's to buy a car "because of the reputation Wal-Mart has." Then the 36-year-old Army chemical and biological operations specialist from Copenhagen, N. Y., spent less than an hour at the dealership picking up a Geo Metro. "I felt good about this because I knew Sam's had checked out the dealer in advance," says Mullaney, who says he bought his Metro for $250 over invoice.

Ultimately, retail analysts predict, consumers will force auto dealers—and manufacturers—to transform or die. For shoppers such as Harriet Grant, 34, of McLean, Va., who recently stormed out of a dealership when a salesman tried to browbeat her into a sale, car dealers' antiquated horse-trading methods couldn't disappear fast enough. "I wish dealerships could work in the same way as when I'm buying an article of clothing," says Grant. That simple plea is shared by millions of frustrated car buyers. And it seems as if they're finally being heard.

By Keith Naughton, with Kathleen Kerwin and Bill Vlasic, in Detroit, Lori Bongiorno and David Leonhardt in New York, and bureau reports

Sport Utilities? Aisle 13

Karen Rezzelle was ready for something different when it came time to buy a new car. Dealers used to insist that her husband's name appear on all the ownership papers, even though she was writing out the check. After her divorce, Rezzelle found the experience even more infuriating. "Is money all you care about?" one salesman brashly inquired after she questioned him on price. But now, the 44-year-old surgical nurse says auto buying is a breeze, thanks to a service she found through her local PriceCostco Inc. warehouse club. "They do everything for you," she says.

Using the substantial purchasing power of its 10 million members, the retailer put together a network of more than 1,000 dealers located anywhere there's a PriceCostco store nearby. They sell virtually every car available, from Mercedes to Chevrolet. Dealers pay a monthly fee to be part of the network and agree to offer PriceCostco members prenegotiated, discounted prices that include options and average about $1,200 less than shoppers could typically get on their own.

"THEY DO EVERYTHING": *Rezzelle landed a Jeep through PriceCostco*

The warehouse club sometimes has cars on display to promote its program, but customers have to buy at a showroom. PriceCostco does have a toehold in new-car sales. It recently began selling custom replicas of the 60s-era Cobra sports car from Milwaukee-based Excalibur Automobile Corp. for $47,650 in a few locations. So far, it has sold three.

Rezzelle picked up a brochure for the service at her local PriceCostco store. She had visited enough showrooms to know what car she wanted, so she called the toll-free number for the name of the nearest network dealer. Besides eliminating the stress of haggling, the service, which is free to PriceCostco members, saves time. "People want to have a very simple, fast, honest way to buy a car," says Walt Green, director of the company's eight-year-old auto program. "That's why there needs to be something like this."

The concept is catching on. Green says 30,900 vehicles were sold to members through the referral service in 1995, triple the number in 1990. Rezzelle's new vehicle was one of them. Last May, she bought a fully loaded Jeep Grand Cherokee in Merced, Calif. The cost: $29,900—$2,000 less than the best price she found on her own. With such savings, traditional auto dealers may soon find themselves on the endangered species list.

By Linda Himelstein in San Francisco

UNLIMITED PARTNERSHIP

THUSTON PACKNETT FROM ARAMARK *with* H.S. GEORGE FROM SAINT JOSEPH HEALTH CENTER

PEOPLE ARE DRIVING

FROM ALL OVER THE KANSAS CITY AREA

TO EAT HOSPITAL FOOD."

o something that had never been done before. That was the challenge I put in front of Thuston. Well, those must be some gic words because you should've seen his eyes light up. I knew right then that the food experience at this hospital would ver be the same. Ideas filled note pad after note pad. And somewhere in those note pads was an inviting and nfortable place where patients and their families could get away from the hospital without ever leaving the hospital. And my surprise, it's also a place people drive to for lunch." Those were the words of H.S. George of Saint Joseph Health nter in Kansas City. "Something that had never been done before." Now that's a powerful phrase. It'll drive you to solve blems, not retro-fit old ideas. In the case of Saint Joseph, a food court right in the middle of a hospital. H S. is happy report that this unexpected idea has caught on. "Just look at the faces of the people eating here. Oh, and also have a nce at the bottom line. Revenues are up 15%. Something that'd never been done before."

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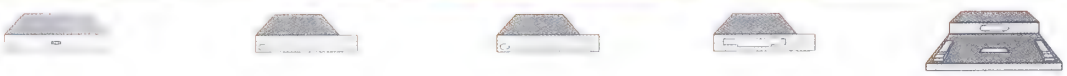

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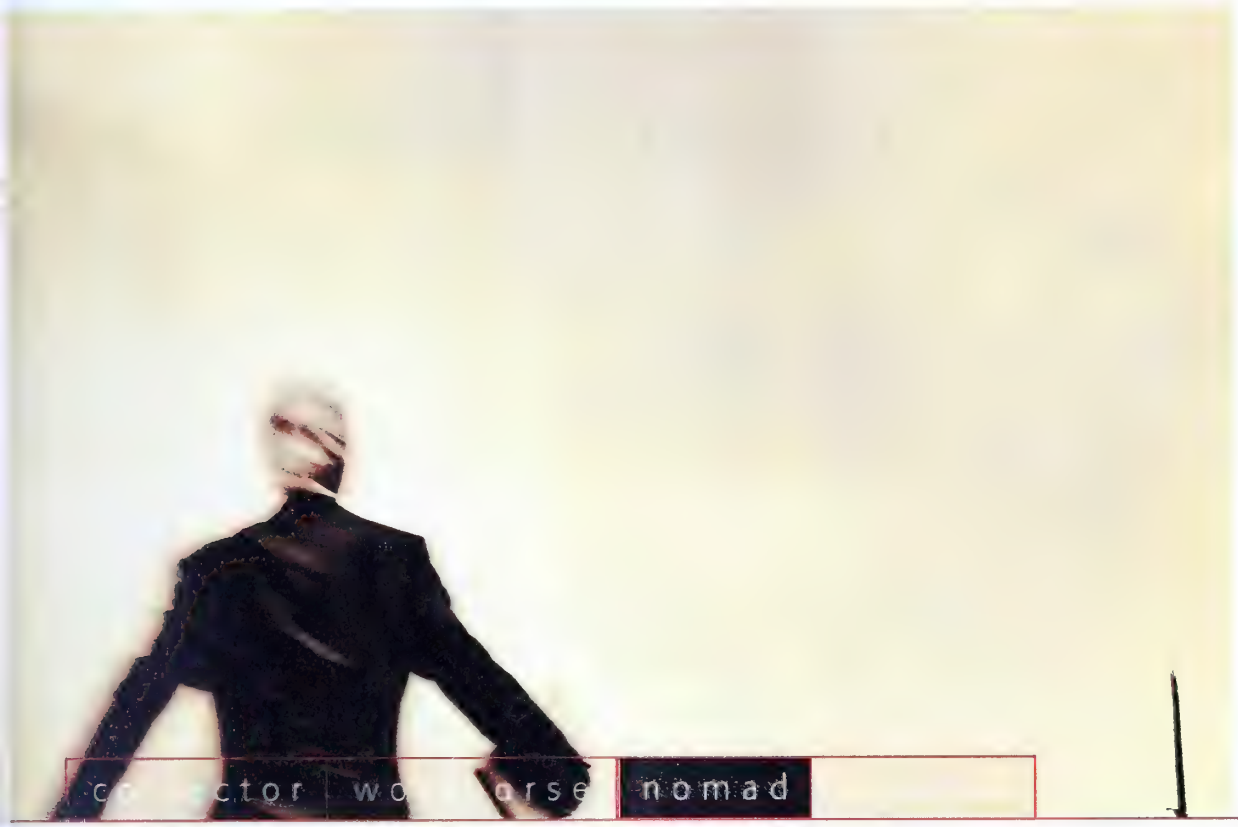


OOK FOR WHOEVER YOU HAPPEN TO BE.

On red-eye flights, you're the only one with the overhead light on. You demand a computer that only needs to recharge when you do.

COMPAQ

Has It Changed Your Life Yet?

COMMENTARY

By Christopher Farrell

A FLAT TAX IS FLAT-OUT RISKY

America's latest tax revolt is gathering momentum. Multimillionaire Steve Forbes has launched his GOP Presidential bid with an all-out assault on the federal income tax. Representative Bill Archer (R-Tex.), the powerful chairman of the House Ways & Means Committee, wants to "pull the income tax out by its roots so it can never grow again." The recent report of the GOP-chartered Tax Reform Commission, chaired by supply-side cheerleader Jack F. Kemp, argues that "the current tax code cannot be revised, should not be reinvented, and must not be retained." It's time, they tell us, to begin anew.

Right now, in the vanguard of the movement to replace the 83-year-old income tax is the 17% flat-rate tax championed by Forbes and House Majority Leader Richard K. Armey (R-Tex.). Thus far, the debate over the flat tax has revolved around the politically explosive question of income distribution. By design, a flat tax reduces the load on the wealthy by exempting from personal taxes interest, dividends, and capital gains. Flat-tax advocates justify the move by claiming a dramatic economic payoff. Although it shied away from endorsing a flat tax, the Kemp Commission predicts a doubling of the nation's growth rate with a switch to a single-rate system.

Sounds good, doesn't it? Problem is, the revolutionaries are wrong. Their florid rhetoric vastly overstates the economic gains and deeply underestimates the risks. There could be a long-term payoff from a flat tax as measured by savings, investment, and growth, but it would be hardly overwhelming. The gains could be easily dwarfed by wrenching business and household upheavals as America shifts to a new tax code.

DOUBLE HIT. Indeed, the transition to a flat tax is fraught with danger—so much so that the long-term payoff may never come. Businesses that borrowed money and invested under the existing income tax rules will suddenly be penalized. So will individuals who saved and bought homes. Businesses will lose interest deductions on borrowed money. Corporate depreciation allowances on existing investments will be wiped out. The stock market will tumble because Corporate America's assets will be worth less.

The flat tax also eliminates deductions for home mortgages. In addition to getting hit on their stock holdings, homeowners will likely suffer a 10% to 15% drop in the value of their homes. The effect on consumer spending could be disastrous. Flat-tax supporters claim that lower interest rates will cushion the drop in the stock market and housing, but it's unlikely rates can fall far enough to offset these downward economic pressures. The initial impact of an Armey-type flat tax could be a recession, says Mark Zandi, economist at Regional Financial Associates Inc. It would take four years for any positive impact from the flat tax to become apparent, he says.

Of course, phasing in the flat tax over a long period of time—sa 30 years—would lessen the ec turmoil. But it creates new qu as well. Any safe harbor chips the promised efficiency gains. policymakers shelter decisions der the old system, the higher gle rate must be, the promised incer work, save, and in more, says William economist at the B Institution. Laurence J. an economis

FLAT TAX
Proponents:
Steve Forbes
Rep. Dick A
and others

USA TAX
Proponents:
Sens. Pete D
and Sam N

NATIONA SALES T OR VALU ADDED T
Proponents:
Rep. Bill Ar
and others

ton Univers gues that wi tion rules "you could end up w savings, investment, and grow with the current income tax."

True, many economists supp principles behind the flat tax. now, corporate earnings are ef taxed at least twice, at the co level and at the individual lev tends to discourage capital spe The flat tax gets rid of double by exempting capital income f sonal taxes, which should, in t

ings and investment. The oth-
ed alternatives to the income
as the Nunn-Domenici USA
larly encourage savings and in-
(table).
will take time for tax incen-
ffect consumer savings. For
more than half of all private
lready are in tax-sheltered
lans, making it unlikely that
ill rise much. Anyway, the big
national savings has been the
udget deficit. The fastest, sur-
o hike America's savings pool
inate the deficit, not to under-
olesale transformation of the
—which at a 17% rate would
deficit into the stratosphere.
se for the proposed flat tax
new investment is more com-
mainly because of changes in
Brinner, economist at DRI/McGraw-Hill.

To be sure, the time is ripe for some reform. Almost everyone agrees that the tax code is riddled with too many exemptions, deductions, exclusions, and credits. The system is expensive, too, with an annual tax-compliance cost of at least $75 billion, says Joel B. Slemrod, economist at the University of Michigan. In the global economy, a simpler tax system would make the U. S. an even more attractive place for business and investors. "Cleaning up the tax code makes us better off," says David Bradford, economist at Princeton University.

MORAL SOCIETY. Why not embrace a progressive, lower-rate income tax system with fewer deductions—but keep the most justifiable deductions, such as charitable contributions and home mortgages? It would be far superior to and all the complexities of the current code is appealing. But a tax system that adjusts to changing economic circumstances and business needs is not a bad thing. In *A History of Taxation and Expenditure in the Western World*, authors Carolyn Webber and Aaron Wildavsky contend that the income tax is "a paradigm of responsive democracy at work." For example, owner-occupied housing offers substantial social benefits in encouraging home and neighborhood maintenance. The charitable contribution deduction is an extremely effective matching-grant system for charities. These tax "loopholes" very much reflect traditional ideas of a good and moral society.

There is a need to cut tax rates for the highest-income taxpayers. The top decile of the population is no longer dominated by what Thorstein B. Veblen called the "leisure class." Today's top 10% is to a large extent made up of entrepreneurs, professionals, and two-earner households. America is still the land of economic mobility. Taxing people by their ability to pay (taking progressively more from the rich and less from the middle class and poor) has proved a remarkably durable idea in American democracy. The rich can afford to pay more, but their rates should come down.

The danger is that radical reform will doom any realistic chance to streamline and simplify the existing tax code. Remember that health-care reform in 1994 was also a laudable goal. But the means for overhauling the health-care system would have been so disruptive that the movement collapsed. This time, policymakers shouldn't blow a chance for real tax reform in the pursuit of single-rate purity. By all means, clean up the code. But don't tear it up.

Economics Editor Farrell covers tax policy.

peting Blueprints for a Tax Revolution

DUALS	TAX ON BUSINESS	MOST CONTROVERSIAL POINTS
7% flat rate on all tion and pension contributions. s are not taxed on other urces, such as interest, and capital gains. No s. Large personal t.	Businesses pay the same rate on gross revenue minus costs of inputs, wages, pension contributions, and corporate capital (immediately expensed). No deductions.	Eliminating charitable, mortgage interest, and state and local deductions. Less progressivity. Very difficult transition.
sive-rate tax on total income vings and investment. ıs for mortgage haritable contributions, education costs. Progressive from 8% to 40%.	Single-rate 11% on gross revenues minus cost of inputs, much like a value-added tax. Immediate write-off for capital investment. Compensation not deductible.	High marginal tax rates. Incentives to hide savings before implementation. Difficult transition. Very complex.
ased consumption tax. With sales tax, a flat percentage ed on to the retail price of services, as with state s. With the VAT, no direct ividuals. Large personal ı with both.	With the VAT, business is taxed at each stage of production. Whether the VAT or the retail sales tax, consumers will pay higher prices for virtually everything they buy.	Taxing services. Reduced progressivity. Transitional incentives to spend. High rates. Potential for widespread evasion.

BOSKIN, ECONOMIST AT STANFORD UNIVERSITY; GOLDMAN SACHS & CO.; AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS; BUSINESS WEEK

ion rules. New investment
t a boost from expensing, an
e 100% first-year tax write-
ı of the gain would show up in
s and buildings; depreciation
ment such as computers al-
quite rapid. Yet in the
ion Age, it's investment in
ı equipment—not more bricks
ar—that matters. At best,
nduced hikes in savings and
nt would raise economic
.1% to 0.2% a year over
decade, estimates Roger
much simpler than what currently exists. The 1986 Tax Act, with three rates topping out at 28% and with no difference between income from work and capital, was a step in the right direction. Similarly, lower the corporate tax rate by eliminating as many industry-specific tax preferences as possible, such as oil and gas allowances. And get rid of the burdensome corporate alternative minimum tax. "There is a lot of room for streamlining, simplification, and rationalization," says Slemrod.

The flat-tax idea of sweeping away

IT'S STILL OPEN SEASON ON CLOSED-END FUNDS

Bargains can be found, but the discounts have been growing narrower

After the spectacular gains made in the stock and bond markets over the past year, a real bargain is hard to find—unless you shop among the closed-end funds. Many of these quirky funds, which invest like mutual funds but are bought and sold like stocks, have racked up stellar investment results in the past year yet still trade at prices that are discounts to their net asset values (NAV). The closed-end fund market is the last place on Wall Street where you can buy $1 in assets for 90¢.

Well, maybe 95¢. There are still bargains among the closed-ends, but they're not as cheap as they were just a few weeks ago. The funds rebounded—NAVs rose, but share prices rose faster—in January, narrowing discounts but certainly not eliminating them.

If you're bargain-hunting in the closed-end mart, remember that buying a fund just because it trades below its NAV is no guarantee of riches. Sometimes discounts get larger, and some funds always seem to trade at a discount. To make a smart choice, you also need to know the fund's NAV returns, the performance of the shares in the market, and the amount of risk the fund takes. That's where BUSINESS WEEK's Mutual Fund Scoreboard for closed-end funds can help.

STRONG START. The scoreboard rates funds based on three-year total NAV return, adjusted for risk. This year, six equity and seven bond funds earned the top rating, three upward-pointing arrows. The ratings and the scoreboard data are prepared by Morningstar Inc., the mutual-fund data company.

As a rule, closed-end fund mavens don't recommend investing in a fund, no matter how good its performance, unless it trades at a discount to its net asset value. In today's market, some of the strongest performers sell at discounts—perhaps a reflection of investor indifference. The Swiss Helvetia Fund, for instance, racked up an impressive 32.2% NAV gain last year, thanks to a bullish equity market and a rising currency. Yet the fund's shares, which trade on the New York Stock Exchange, gained only 20%. During the year, the fund traded at prices that were nearly a 16% discount to NAV—the greatest price-to-NAV gap in six years. So far this year, the discount has narrowed to 10%.

The Best Closed-End Funds

These funds have earned three upward-pointing arrows, the highest rating for risk-adjusted total return for the 1993–95 period.

	AVERAGE ANNUAL TOTAL RETURN*	RISK	INVESTMENT CATEGORY
EQUITY FUNDS			
CENTRAL SECURITIES	26.7%	Low	U.S.
CHILE	25.5	High	Latin America
FIRST FINANCIAL	35.6	Low	U.S.
IRISH INVESTMENT	22.4	Average	Europe
KOREA	26.9	High	Pacific
SWISS HELVETIA	24.8	Low	Europe
BOND FUNDS			
ACM MANAGED INCOME	16.5	High	Multisector
APEX MUNICIPAL	7.9	Very low	Municipal
COLONIAL MUNICIPAL INCOME	6.3	Very low	Municipal
FRANKLIN UNIVERSAL	13.5	Average	Multisector
MFS MUNICIPAL INCOME	7.6	Very low	Municipal
NEW AMERICA HIGH INCOME	17.1	Low	Corp.-High-Yield
NUVEEN NY PERFORM. PLUS MUNI.	9.0	Low	Municipal

*1993–95, pretax return based on appreciation of net asset value plus reinvestment of dividends and capital gains

DATA: MORNINGSTAR INC.

Most closed-end equity funds invest abroad—and nearly all foreign markets trailed the U.S. last year. So it comes as no surprise that the average closed-end equity fund lagged its equity mutual-fund cousin during 1995. But many investment analysts expect foreign markets—and hence, closed-end equity funds—to outperform the U.S. market in '96. They're off to a strong start. Thomas J. Herzfeld, a Miami investment manager who specializes in closed-end funds, says his international-fund portfolio rose 11% in January alo

The outlook is still bright for clos end bond funds, even though they an outstanding 1995. They earned average 22.1% total return on tl portfolios, vs. 16.4% for bond mu funds. The main reason is that m closed-end funds leverage their port os through margin borrowings or issu preferred stock. That means a fund $200 million in shareholder money own perhaps $300 million in bonds. leverage can be brutal when the b market tanks, but it pays off in spa when bond prices rise.

leverage works well for yi seekers, since those ex bonds help funds gene higher yields than their leveraged kin.

FLAT-TAX FEAR. In a l interest-rate environm these funds still make c pelling buys. Fund ana Robert A. Young of D Witter Reynolds Inc. s even after the January co back, leveraged muni fu trade at a hefty 7.5% disc to NAV. Of course, the n funds are somewhat in dumps because of the that a flat tax will be enac wiping out munis' tax ad tage and slashing prices munis yield the same as ables (BW—Feb. 13).

But if you're not afrai the flat tax—most exp think it's a long shot—t funds are attractive. Morningstar lyst Gregg Wolper estimates that wi leveraged muni fund, an investor pick up 0.5% to 1% more yield ov bond mutual fund. One of Young's re mendations is BlackRock Investm Quality Municipal Trust, with a 1 discount and a 6.2% yield. That's equivalent of 9% for an investor in 31% marginal tax bracket—a pretty return all by itself. And if the disc narrows, that's just icing on the cak

By Jeffrey M. Laderman in New

UTUAL FUND SCOREBOARD

Closed-End Equity Funds

	RATING	CATEGORY	RISK	SIZE	FEES	1995 RESULTS					TREND	PREMIUM/DISCOUNT	
						NAV RET (%)		SHARES RET (%)				DIFFERENCE FROM NAV	
				ASSETS $MIL	EXPENSE RATIO (%)	1 YR.	3 YRS.	1 YR.	3 YRS.	YIELD (%)	3-YEAR ANALYSIS	1995 HIGH-LOW	2/2/96
AMS EXPRESS	▲	U.S.	Low	986.2	0.33	29.8	12.0	29.4	7.6	2.7		–10.3- –15.7	–13.4
LIANCE GLOBAL ENVIRONMENT	▼	World	Average	91.2	1.57	19.4	5.2	16.0	1.8	0.2		–18.1- –26.6	–21.1
GENTINA FUND	▼▼	Latin America	High	108.9	1.87	3.3	10.3	–2.4	1.2	2.9		15.7- –7.0	8.5
A LIMITED	▼▼	World	Very high	332.7	0.53	–26.2	13.4	–13.3	10.2	4.6		21.4- –13.3	3.6*
IA PACIFIC	AVG	Pacific	High	268.1	2.06	5.7	19.4	4.6	11.8	0.3		18.9- –9.9	3.1
IA TIGERS		Pacific		253.3	1.65	4.8	NA	19.7	NA	0.9		–4.1- –17.1	–1.4
STRIA FUND	AVG	Europe	Average	120.5	1.71	11.7	13.8	4.7	9.2	0.0		–10.0- –22.9	–14.2
KER FENTRESS	▲▲	U.S.	Low	599.2	0.75	36.7	14.5	33.5	12.2	2.0		–16.7- –23.3	–19.7
RGSTROM CAPITAL	AVG	U.S.	Average	149.4	0.84	41.9	13.2	34.9	–1.3	0.9		–9.5- –16.6	–10.4
UE CHIP VALUE	▲▲	U.S.	Low	92.9	1.22	38.8	16.5	42.4	12.0	1.4		–8.0- –15.4	–8.4
AZIL FUND	▲	Latin America	Very high	336.4	1.71	–23.7	23.7	–26.6	26.1	1.4		14.2- –14.7	5.2*
AZILIAN EQUITY	AVG	Latin America	Very high	66.7	1.86	–27.0	22.5	–29.5	23.9	0.0		18.4- –7.8	7.6*
NTRAL EUROPEAN EQUITY (a)	▲▲	Europe	Average	247.7	1.14	15.8	18.6	16.6	14.1	2.3		–16.4- –24.7	–18.6
NTRAL FUND OF CANADA	▼▼	U.S.	Average	81.4	0.92	2.1	6.6	–3.8	8.3	0.2		8.0- –6.6	3.4*
NTRAL SECURITIES	▲▲▲	U.S.	Low	292.5	0.65	36.8	26.7	48.4	35.0	1.5		3.4- –7.0	5.0*
ILE FUND	▲▲▲	Latin America	High	370.3	1.39	4.3	25.5	16.7	22.2	2.8		–1.7- –19.7	–6.1
INA FUND	▼▼	Pacific	High	132.6	2.55	–2.2	0.0	–6.9	2.6	0.0		20.3- –7.4	10.7
EMENTE GLOBAL GROWTH	AVG	World	Average	62.8	1.75	–0.8	10.1	–1.5	8.5	0.0		–17.0- –25.1	–18.8*
HEN & STEERS TOTAL RETURN		U.S.		99.4	1.31	9.2	NA	16.5	NA	7.2		5.5- –5.1	3.7
UNSELLORS TANDEM	▼	U.S.	Average	81.4	1.30	36.5	6.7	38.5	9.0	1.0		–9.1- –15.9	–8.2
LAWARE GROUP DIV. & INCOME		Income		200.6	1.77	23.2	NA	35.3	NA	8.2		1.5- –9.6	1.0
LAWARE GROUP GLOBAL DIV.		Income		94.2	1.32	21.5	NA	33.2	NA	8.4		–1.5- –9.6	–2.3
FF & PHELPS UTILITIES INCOME	▼	Income	Average	2239.3	1.18	33.7	6.8	24.6	5.0	8.0		16.7- 1.0	6.7
ERGING GERMANY	▼	Europe	Average	128.9	1.40	–1.3	7.8	–1.7	4.9	0.0		–16.9- –27.0	–20.2
ERGING MKTS. INFRASTRUCTURE		World		190.1	2.02	–8.9	NA	3.4	NA	1.0		–10.6- –20.4	–10.4
ERGING MARKETS TELECOMM.	▲	World	Average	154.5	1.89	–1.5	18.0	–8.1	13.0	0.3		–0.8- –16.8	–7.7
ERGING MEXICO	▼▼▼	Latin America	Very high	70.0	1.75	–24.7	–11.5	–48.2	–15.5	0.0		40.7- –13.1	–6.9*
ERGING TIGERS		Pacific		310.1	1.32	0.9	NA	14.7	NA	0.4		–6.2- –16.5	–5.7
UUS II	AVG	U.S.	Low	63.3	2.23	20.7	8.9	17.6	17.7	0.1		–28.6- –37.3	–31.0
ROPE FUND	▲▲	Europe	Low	144.2	1.42	22.0	18.5	26.8	17.3	6.9		–4.8- –15.7	–6.0
ROPEAN WARRANT	▲	Europe	High	84.0	1.74	23.7	22.9	21.4	16.1	0.0		5.0- –22.2	–13.7*
ELITY ADVISOR EMERG. ASIA		Pacific		121.3	1.79	–1.6	NA	7.7	NA	0.5		–7.7- –16.7	–7.0
ST AUSTRALIA	▼	Pacific	High	167.2	1.50	2.6	12.9	–0.4	9.9	3.2		–7.2- –19.5	–10.5
ST FINANCIAL	▲▲▲	U.S.	Low	185.3	1.58	52.9	35.6	62.5	36.5	0.9		8.8- –5.3	–0.8
ST IBERIAN	AVG	Europe	Average	66.6	2.02	18.0	14.8	9.8	10.3	0.9		–18.1- –24.7	–20.4
ST ISRAEL	▼▼▼	World	High	67.0	2.64	24.6	–1.3	14.8	–2.0	0.0		9.0- –14.9	–9.4
ST PHILIPPINE	▼	Pacific	High	193.4	1.82	–24.3	16.7	–25.7	17.9	0.0		–12.7- –24.5	–15.1
ANCE GROWTH	▼	Europe	Average	182.0	1.63	13.7	9.6	17.0	8.7	4.0		–12.2- –21.2	–12.7
BELLI EQUITY	▲	U.S.	Low	1034.1	1.19	19.5	13.8	10.7	12.9	5.7		5.9- –11.9	–8.0
BELLI GLOBAL MULTIMEDIA		World		89.6	1.74	11.1	NA	–2.2	NA	3.7		6.4- –19.3	–13.5
MINI II CAPITAL	AVG	U.S.	Average	287.8	NA	38.4	15.1	46.1	23.3	0.0		–2.2- –15.6	–7.9
MINI II INCOME	▲▲	Income	Very low	101.9	NA	12.6	14.6	8.5	8.2	14.9		19.2- 8.1	11.9
NERAL AMERICAN INVESTORS	▼	U.S.	Average	573.7	1.17	23.6	5.7	21.2	–2.1	0.5		–10.8- –18.1	–16.6
RMANY FUND	▲▲	Europe	Average	189.7	1.28	14.9	18.5	15.9	10.6	8.6		–10.4- –20.1	–14.7
OBAL HEALTH SCIENCES	▲▲	U.S.	Average	427.5	1.33	67.3	17.4	68.4	14.6	0.0		–17.2- –22.2	–15.4
EATER CHINA	▼▼	Pacific	Very high	139.3	2.08	2.3	5.8	17.2	7.6	0.6		0.8- –16.7	–0.3
OWTH FUND OF SPAIN	▲▲	Europe	Average	223.9	1.23	23.3	17.9	20.6	16.3	3.8		–15.5- –25.1	–15.8
. GLOBAL DEVELOPING MKTS.		World		422.3	2.01	0.2	NA	7.5	NA	7.5		–11.4- –22.9	–10.5
. GREATER EUROPE	AVG	Europe	Average	238.7	1.87	7.1	14.3	6.8	14.3	1.0		–11.0- –17.2	–9.1
Q HEALTHCARE INVESTORS	▼	U.S.	Average	134.9	1.76	59.6	9.9	58.8	7.3	0.0		–8.7- –18.9	–9.0

of 2/1/96. ** As of 1/31/96. NA = Not available.
Formerly Future Germany.

DATA: MORNINGSTAR, INC., CHICAGO, IL.

w to Use the Tables

ed-end funds are publicly
ed investment companies.
' results are measured two
: one, by the change in net
t value (NAV), which is gener-
by the fund's manager; the
', by the change in the
es' market price. Total
ns, which include dividends
capital gains, are shown for
and three-year periods. The
e-year figure is an average an-
return. All returns are pretax.

INESS WEEK RATING

ngs are based on three-year
adjusted performance of the
's portfolio. A rating is calculated by subtracting a fund's risk-of-loss factor from total return. Equity funds are rated against each other, and to earn an above-average rating, must beat the S&P 500 on a risk-adjusted basis. For ratings, municipal bond funds are separated from other bond funds.

▲ ▲ ▲ SUPERIOR
▲ ▲ VERY GOOD
▲ GOOD
AVG AVERAGE
▼ BELOW AVERAGE
▼ ▼ POOR
▼ ▼ ▼ VERY POOR

RISK

For each fund, the monthly Treasury bill return is subtracted from the monthly NAV return in each month of the rating period. When a fund has underperformed Treasury bills, this monthly result is negative. The sum of these negative numbers is then divided by the number of months. The result is a negative number, and the greater its magnitude, the higher the risk of loss.

EXPENSE RATIO

Fund expenses for 1995 as a percent of average net assets. Ratio may include interest expense.

YIELD

Income earned during 1995, as a percentage of yearend NAV per share, adjusted for capital gains.

MATURITY

The average maturity of the securities in a bond fund, weighted according to their market value.

TREND

A fund's relative performance during 1993, 1994, and 1995. From left to right, the level of green in each shows how the portfolio of each fund performed relative to other funds: ■ for the top quartile; ■ for the second quartile; ■ for the third quartile; and □ for the bottom quartile. An empty box indicates no returns for that time period.

PREMIUM/DISCOUNT

The market price of closed-end funds is either less than the value of their securities, a discount, or more, a premium, to their NAVs.

MUTUAL FUND SCOREBOARD

Closed-End Equity Fun

	RATING	CATEGORY	RISK	SIZE	FEES	1995 RESULTS					TREND	PREMIUM/DISCOUNT	
				ASSETS	EXPENSE	NAV RET. (%)		SHARES RET. (%)		YIELD	3-YEAR	DIFFERENCE FROM NAV	
				$MIL.	RATIO (%)	1 YR	3 YRS.	1 YR	3 YRS.	(%)	ANALYSIS	1995 HIGH-LOW	2/2/96
H&Q LIFE SCIENCES INVESTORS	▼▼	U.S.	Average	113.9	1.83	64.7	6.6	66.7	4.8	0.0		-10.3- -19.2	-12.3
INDIA FUND		Pacific		392.7	1.98	-35.8	NA	-16.5	NA	0.0		5.8- -26.1	16.2
INDIA GROWTH	▼▼▼	Pacific	Very high	104.1	1.94	-36.9	1.4	-25.7	7.2	0.0		22.7- -5.8	23.3
IRISH INVESTMENT	▲▲▲	Europe	Average	69.0	1.74	37.3	22.4	39.4	22.8	1.2		-10.1- -23.2	-7.4
ITALY FUND	▼▼	Europe	High	86.0	1.69	-3.6	7.5	-5.9	4.2	0.3		-4.6- -16.2	-11.1
JAPAN EQUITY	▼	Pacific	High	121.8	0.97	-3.3	15.3	9.0	28.7	0.8		28.8- -5.4	18.3
JAPAN OTC EQUITY	▼▼	Pacific	High	90.4	1.42	-21.6	4.7	-10.3	4.7	0.0		23.4- -7.5	13.4
JARDINE FLEMING CHINA REGION	▼▼▼	Pacific	Very high	101.6	2.01	-10.4	-3.4	-10.3	-3.2	0.9		10.5- -14.9	2.6
JARDINE FLEMING INDIA		Pacific		115.9	2.29	-40.4	NA	-26.2	NA	0.1		15.5- -15.3	25.3
JOHN HANCOCK BANK & THRIFT		U.S.		628.9	1.49	46.3	NA	56.0	NA	0.0		-5.9- -16.7	-14.3
JOHN HANCOCK PAT. GLOBAL DIV.	AVG	Income	Low	176.0	1.26	31.3	11.1	45.0	9.6	8.2		-2.7- -13.0	-5.7
JOHN HANCOCK PAT. PREF. DIV.		Income		149.8	1.30	30.2	NA	36.3	NA	9.0		-0.5- -7.2	1.0
JOHN HANCOCK PAT. PREM. DIV. I	▼	Income	Average	211.6	1.32	34.9	9.1	36.9	8.3	8.5		5.9- -6.7	-1.9
JOHN HANCOCK PAT. PREM. DIV. II	▼	Income	Average	282.3	1.27	38.5	10.1	37.4	9.2	8.8		0.5- -11.8	-4.9
JOHN HANCOCK PAT. SELECT DIV.	▼	Income	Low	224.6	1.29	34.4	9.2	32.8	2.4	8.8		0.6- -9.7	-2.3
KOREA FUND	▲▲▲	Pacific	High	747.1	1.32	4.3	26.9	5.9	20.1	0.0		13.5- -5.2	6.3
KOREA EQUITY		Pacific		76.4	1.67	-7.2	NA	-5.5	NA	0.2		-0.1- -17.8	-0.4
KOREAN INVESTMENT	▼▼	Pacific	High	91.5	2.00	-22.5	4.8	-18.4	0.2	2.9		1.1- -15.1	-3.2
LATIN AMERICA EQUITY	▼	Latin America	High	128.4	1.70	-15.2	12.2	-25.7	7.8	0.9		4.5- -18.0	-1.9
LATIN AMERICA INVESTMENT	▼▼	Latin America	High	134.3	1.72	-14.3	10.3	-20.3	8.1	0.2		1.5- -17.4	-4.0
LATIN AMERICAN DISCOVERY	▼▼▼	Latin America	Very high	127.6	2.15	-30.1	4.2	-40.9	6.1	0.0		11.4- -20.0	-3.2
LIBERTY ALL-STAR EQUITY	▲	U.S.	Low	854.2	1.07	31.9	12.2	43.8	10.5	4.8		-1.3- -9.1	-3.4
LIBERTY ALL-STAR GROWTH (b)	AVG	U.S.	Very low	119.6	1.51	16.4	7.9	21.3	4.8	4.7		-10.6- -18.0	-15.0
MALAYSIA FUND	▼	Pacific	High	180.6	1.19	4.0	17.9	2.5	14.7	0.0		3.6- -12.8	0.2
MEXICO FUND	▼▼▼	Latin America	Very high	750.3	1.14	-20.3	-10.5	-38.9	-13.0	0.2		23.1- -21.7	-7.8
MEXICO EQUITY & INCOME	▼▼▼	Latin America	Very high	86.3	1.64	-11.9	-2.4	-40.7	-4.4	0.9		43.1- -14.1	-9.8
MFS SPECIAL VALUE	▲▲	U.S.	Low	87.1	1.26	33.5	15.3	37.6	20.0	3.4		19.7- 6.9	12.4
MORGAN GRENFELL SMALLCAP	AVG	U.S.	Average	87.3	1.52	41.5	14.6	42.3	8.7	0.0		-10.3- -19.0	-10.0
MORGAN STANLEY AFRICA INVESTMT.		World		263.5	1.87	27.2	NA	21.8	NA	7.5		-16.5- -25.8	-17.2
MORGAN STANLEY ASIA-PACIFIC		Pacific		769.4	1.31	9.2	NA	9.8	NA	0.4		-6.7- -23.2	-5.9
MORGAN STANLEY EMERG. MKTS.	AVG	World	Average	332.7	1.75	-16.3	15.5	-17.7	14.6	0.0		15.3- -8.9	8.7
MORGAN STANLEY INDIA INVEST.		Pacific		317.1	1.61	-36.5	NA	-18.9	NA	0.0		9.1- -24.9	24.1
NEW AGE MEDIA		U.S.		268.8	1.35	44.7	NA	49.5	NA	0.4		-12.7- -24.0	-15.4
NEW GERMANY	AVG	Europe	Average	496.2	1.02	8.8	13.8	4.7	9.1	3.5		-16.4- -25.1	-20.4
NEW SOUTH AFRICA		World		93.9	2.10	21.8	NA	11.9	NA	5.0		-14.2- -24.0	-15.8
PAKISTAN INVESTMENT		Pacific		76.1	1.93	-42.5	NA	-41.6	NA	0.1		-11.8- -29.2	-8.3
PETROLEUM & RESOURCES	AVG	U.S.	Low	401.4	0.42	26.7	12.7	21.2	12.2	3.0		-3.0- -10.4	-8.5
PILGRIM REGIONAL BANKSHARES	▲▲	U.S.	Low	209.8	1.28	49.8	16.0	52.9	13.2	2.5		-9.6- -16.2	-14.3
PORTUGAL FUND	AVG	Europe	Average	70.4	1.41	-5.8	15.0	-18.5	12.4	1.3		-2.9- -17.7	-12.7
PREFERRED INCOME	▲	Income	Very low	210.4	1.55	23.5	10.5	17.1	2.9	8.4		0.6- -13.4	-12.4
PREFERRED INCOME MANAGEMENT		Income		212.5	1.91	27.7	NA	23.8	NA	8.7		-1.1- -13.5	-11.5
PREFERRED INCOME OPPORTUNITY	▲	Income	Very low	205.4	1.69	25.4	11.0	17.1	3.3	8.7		-0.1- -14.5	-12.3
PUTNAM DIVIDEND INCOME	AVG	Income	Very low	116.7	1.07	17.3	8.7	17.5	1.7	7.8		-8.4- -14.8	-9.6
QUEST FOR VALUE CAPITAL	AVG	U.S.	Average	605.8	NA	30.7	12.5	38.8	15.6	0.0		-5.3- -14.5	-7.8
QUEST FOR VALUE INCOME	▲▲	Income	Very low	209.4	0.74	12.0	11.2	10.9	8.3	11.6		6.8- 2.2	4.3
ROC TAIWAN	▼▼	Pacific	High	314.5	1.99	-29.3	3.3	-11.6	6.7	0.0		18.5- -17.3	6.1
ROYCE MICRO-CAP		U.S.		100.1	1.88	22.6	NA	19.5	NA	4.5		1.7- -16.1	-14.6
ROYCE VALUE	▲	U.S.	Very low	339.0	2.00	21.9	12.7	19.8	8.6	0.2		-4.2- -15.4	-9.3
SALOMON BROS.	▲▲	U.S.	Low	1354.4	0.49	36.7	16.0	45.3	14.2	2.4		-13.3- -19.1	-10.4
SCHRODER ASIAN GROWTH		Pacific		255.0	1.65	1.1	NA	17.1	NA	0.0		-3.8- -18.0	-4.9
SCUDDER NEW ASIA	AVG	Pacific	Average	132.9	1.67	-1.2	14.6	-0.4	13.9	0.1		7.7- -10.5	9.8
SCUDDER NEW EUROPE	▲	Europe	Average	210.0	1.67	19.0	14.2	23.8	14.0	0.4		-11.7- -22.3	-16.9
SINGAPORE FUND	▲	Pacific	Average	120.6	2.01	5.3	20.7	2.4	28.0	2.1		14.5- -7.1	7.8
SOURCE CAPITAL	AVG	U.S.	Very low	362.1	0.96	20.6	8.9	23.5	4.6	6.1		3.2- -5.7	-2.8
SOUTHERN AFRICA		World		127.7	2.30	31.5	NA	28.8	NA	3.4		-12.9- -24.2	-15.1
SPAIN FUND	▼	Europe	Average	108.2	2.09	15.3	11.4	6.5	3.1	0.4		-10.7- -20.1	-14.2
SWISS HELVETIA	▲▲▲	Europe	Low	306.2	1.57	32.2	24.8	20.0	21.1	1.8		-1.8- -15.9	-10.0
TAIWAN FUND	▼▼	Pacific	High	282.6	2.43	-22.6	9.1	-7.9	12.6	0.0		22.3- -20.7	15.4
TCW/DW EMERGING MARKETS OPPORT.		World		251.6	1.73	-6.6	NA	-4.5	NA	0.2		-8.5- -21.4	-7.0
TEMPLETON CHINA WORLD		Pacific		239.7	1.65	7.9	NA	9.9	NA	3.1		10.5- -18.3	-2.8
TEMPLETON DRAGON		Pacific		785.8	1.54	11.7	NA	19.7	NA	3.5		-8.1- -19.4	-11.9
TEMPLETON EMERGING MARKETS	▲	World	Average	241.6	1.73	-6.0	18.9	8.2	21.6	1.3		25.8- 4.1	24.1
TEMPLETON VIETNAM OPPORT.		Pacific		107.0	1.72	5.1	NA	2.7	NA	3.3		4.5- -21.5	-0.0
THAI FUND	▲	Pacific	High	313.3	1.22	1.6	22.2	15.4	21.9	0.4		-6.2- -20.5	-2.2
THAI CAPITAL	AVG	Pacific	High	108.8	2.12	-0.7	21.3	8.5	20.1	0.0		-4.1- -18.0	-4.1
TRI-CONTINENTAL	▲	U.S.	Low	2506.8	0.64	34.4	12.8	31.4	8.9	5.5		-14.6- -19.1	-16.8
UNITED KINGDOM FUND	▲	Europe	Low	58.5	1.47	18.1	15.7	15.2	12.6	3.2		-11.5- -19.2	-17.4
WORLDWIDE VALUE	▲	World	Low	62.2	2.10	19.3	14.3	18.9	12.4	0.4		-17.4- -24.3	-15.7
ZWEIG	AVG	U.S.	Low	547.9	1.25	15.3	8.4	16.8	4.2	0.6		10.3- -2.6	-0.3
ZWEIG TOTAL RETURN	AVG	Income	Very low	647.5	1.12	16.5	8.2	16.4	4.2	5.6		6.2- -1.5	1.0

* As of 2/1/96. ** As of 1/31/96. NA = Not available
(b) Formerly Charles Allmon Trust.

DATA: MORNINGSTAR, INC., CHICAGO

Closed-End Bond Funds

	RATING	CATEGORY	RISK	SIZE	FEES	1995 RESULTS				PORTFOLIO		TREND	PREMIUM/DISCOUNT	
				ASSETS $MIL.	EXPENSE RATIO (%)	NAV RET (%) 1 YR	NAV RET (%) 3 YRS	MARK. RET (%) 1 YR	MARK. RET (%) 3 YRS	YIELD (%)	MAT. (YRS.)	3-YEAR ANALYSIS	1995 HIGH-LOW	2/2/96
A GOVERNMENT INCOME	◆◆	Multisector	Very high	557.6	1.60	28.8	10.0	11.3	6.3	10.7	10.0		17.6—6.6	–1.7
A GOVERNMENT SECURITIES	◆◆	Multisector	Very high	729.3	1.52	29.3	9.4	14.0	4.5	11.6	9.0		10.0– –12.0	–6.8
A GOVERNMENT SPECTRUM	◆◆◆	Multisector	Very high	276.7	1.21	21.6	7.0	4.4	2.6	11.9	10.8		12.8– –11.3	–3.5
A MANAGED DOLLAR INCOME		International		311.9	1.78	29.8	NA	16.0	NA	13.3	15.1		13.5– –11.4	–4.8
A MANAGED INCOME	◆◆◆	Multisector	High	284.3	1.07	36.8	16.5	23.4	12.5	11.5	12.1		17.3– –1.2	2.5
A MUNICIPAL SECURITIES		Municipal		226.1	0.77	25.3	NA	37.7	NA	7.1	27.1		–0.2– –6.8	1.9
-AMERICAN TERM		Corp General		193.9	1.05	18.5	NA	18.8	NA	8.8	9.4		–6.3– –14.6	–7.1*
IANCE WORLD DOLLAR GOVT. II		International		868.9	1.28	23.1	NA	31.4	NA	12.5	21.5		13.9– –6.4	0.4
ERICAN STRAT. INCOME II	◆	Corp General	High	261.9	1.27	21.8	8.5	3.9	–1.0	10.8	16.0		–1.1– –17.9	–15.6*
ERICAN STRAT. INCOME III		Corp General		333.6	1.29	18.3	NA	13.8	NA	10.9	14.3		–0.2– –16.0	–13.6*
X MUNICIPAL	◆◆◆	Municipal	Very low	198.2	0.91	13.4	7.9	7.8	4.1	8.0	20.7		–3.9– –14.9	–7.5
INCOME	◆◆	Corp General	Low	207.8	0.83	18.5	11.1	24.3	8.1	9.7	6.3		–4.8– –13.3	–2.0
CKROCK 1998 TERM TRUST	◆	Government	Average	565.1	0.90	15.7	5.4	17.8	3.2	6.0	NA		–3.1– –10.8	–8.8*
CKROCK 2001 TERM TRUST	◆	Government	High	1241.8	0.63	20.1	6.4	14.4	2.0	6.7	NA		–6.4– –18.1	–16.0*
CKROCK CA INSURED 2008	◆◆	Municipal	Very high	231.3	1.08	23.8	10.3	20.7	5.5	6.3	14.8		–3.0– –14.4	–12.8
CKROCK INCOME	◆◆	Government	High	477.5	1.10	21.7	5.8	15.8	0.8	11.8	NA		–2.0– –19.3	–17.2*
CKROCK INSURED MUNI. 2008	◆◆	Municipal	Very high	612.1	1.02	23.7	10.8	17.7	5.9	6.7	14.4		–4.3– –16.0	–11.5
CKROCK INSURED MUNI. TERM	◆	Municipal	High	406.7	1.04	20.7	10.4	25.4	7.1	6.3	14.0		–5.1– –10.6	–7.4
CKROCK INVEST. QUAL. MUNI.		Municipal		352.3	1.14	32.3	NA	26.9	NA	6.8	21.8		–6.9– –17.7	–14.3
CKROCK INVEST. QUAL. TERM	◆	Government	High	337.8	0.94	25.2	8.3	22.0	2.5	8.0	NA		–12.1– –18.7	–17.5*
CKROCK MUNICIPAL TARGET	AVG	Municipal	Average	722.7	0.94	19.1	10.2	21.7	6.8	6.4	11.0		–5.1– –11.2	–6.4
CKROCK NY INSURED 2008	◆◆	Municipal	Very high	253.3	1.08	24.2	10.4	24.2	8.4	5.9	15.2		–4.4– –9.7	–7.5
CKROCK NORTH AMER. GOVT.	◆◆◆	International	Very high	404.5	1.01	32.1	6.8	23.4	0.8	3.4	NA		–2.4– –17.5	–12.7*
CKROCK STRATEGIC TERM	◆	Government	High	512.8	0.98	23.6	6.6	15.2	–0.7	7.4	NA		–8.2– –19.5	–18.5*
CKROCK TARGET TERM	◆	Government	High	930.8	0.75	20.1	6.9	16.5	3.2	8.0	NA		–3.2– –13.7	–11.2*
NA HIGH-INCOME	◆◆	Corp Hi Yld	Very low	259.8	3.27	22.2	13.8	26.0	12.8	10.7	8.1		12.5– –1.4	10.0
ONIAL HIGH-INC MUNICIPAL	◆◆	Municipal	Very low	263.2	1.03	15.8	7.1	15.7	4.1	8.0	23.4		–3.4– –13.7	–5.0
ONIAL MUNICIPAL INCOME	◆◆◆	Municipal	Very low	202.7	0.90	13.5	6.3	14.2	4.5	7.9	22.8		0.5– –12.3	–7.0
IPORATE HIGH YIELD		Corp Hi Yld		294.0	2.53	26.4	NA	32.7	NA	11.0	8.7		5.6– –1.9	3.6
N WITTER GOVT. INCOME	AVG	Government	Very low	478.5	0.71	16.7	7.1	15.8	4.9	6.7	9.3		–8.2– –12.8	–8.9
YFUS MUNICIPAL INCOME	AVG	Municipal	Low	195.5	0.85	17.0	7.3	11.7	2.7	7.0	23.8		3.0– –9.4	1.1
YFUS STRAT. MUNI. BOND	AVG	Municipal	Low	431.2	0.86	17.5	7.1	16.9	3.5	7.0	22.7		1.4– 8.3	–1.6
YFUS STRAT. MUNICIPALS	◆◆	Municipal	Very low	559.6	0.87	15.1	7.8	11.8	4.3	7.3	21.8		4.3– –6.4	–1.4
F & PHELPS UTIL. TAX-FREE	◆	Municipal	Average	202.8	1.35	24.7	10.8	30.7	7.1	6.7	19.7		–4.7– –11.5	–1.9
F & PHELPS UTIL. & CORP.		Corp General		352.7	2.24	32.9	NA	36.3	NA	8.5	20.9		0.1– –9.2	–2.9
RGING MKTS. INCOME II		International		244.1	2.40	34.6	NA	38.6	NA	13.8	12.1		28.1– –0.5	4.2
ST AUSTRALIA PRIME INCOME	◆◆	International	Very high	1925.3	1.47	11.3	11.5	26.8	8.9	10.2	7.0		3.4– –11.4	–2.0
NKLIN UNIVERSAL	◆◆◆	Multisector	Average	255.4	2.26	26.5	13.5	27.9	12.7	9.4	9.2		–2.9– –9.0	–5.7
BAL HIGH INCOME DOLLAR		International		301.3	1.50	24.8	NA	22.9	NA	11.2	14.3		–2.7– –15.8	–10.1
ENWICH STREET MUNI.		Municipal		245.7	1.05	23.6	NA	29.9	NA	5.8	26.3		–4.3– –11.0	–5.3
H INCOME ADVANTAGE II	◆	Corp Hi Yld	Low	209.4	0.93	15.5	11.8	18.9	13.0	10.9	7.7		6.5– –2.1	2.4
H INCOME OPPORTUNITY		Corp Hi Yld		793.7	1.15	19.6	NA	19.7	NA	10.8	7.8		–0.7– –9.6	–4.7
ERION 1997 TERM	◆◆◆	Government	Average	478.0	3.17	7.9	1.5	5.1	–3.1	7.2	8.2		–2.9– –10.5	–8.2*
ERION 1999 TERM	◆◆◆	Government	High	508.2	2.52	7.2	3.5	7.7	–5.2	7.7	11.9		–8.2– –15.6	–10.7*
ERION 2002 TERM	◆	Government	Average	304.1	3.20	23.1	6.2	22.8	–0.8	7.6	15.2		–12.0– –17.8	–16.2*
ERION TOTAL RETURN	◆◆	Multisector	Low	256.8	2.84	24.5	10.8	24.6	3.3	10.1	12.2		–10.1– –17.5	–11.7*
OME OPPORTUNITIES 1999	◆	Government	Average	470.7	2.80	23.1	7.6	19.2	3.1	6.1	13.7		–7.1– –16.1	–11.8
URED MUNICIPAL INCOME		Municipal		412.4	1.74	33.0	NA	29.1	NA	6.1	27.1		–12.0– –19.8	–16.3
ERCAPITAL CA INSURED MUNI.		Municipal		255.3	0.89	31.5	NA	12.5	NA	6.5	25.7		–4.3– –17.6	–13.0
ERCAPITAL CA QUALITY MUNI.		Municipal		214.6	0.93	36.9	NA	24.2	NA	6.6	25.5		–9.1– –19.3	–15.4
ERCAPITAL INCOME SEC.	AVG	Corp General	Average	223.5	0.69	19.4	8.9	14.3	2.9	9.0	22.4		4.7– –10.7	–2.7
ERCAPITAL INS. MUNI. INC.		Municipal		626.3	0.80	32.1	NA	15.8	NA	6.7	25.3		–9.6– –18.4	–15.7
ERCAPITAL INS. MUNI.	◆	Municipal	High	496.3	0.77	22.1	10.4	24.6	6.6	6.8	25.7		–3.8– –8.9	–6.8
ERCAPITAL QUAL. MUNI. INC.	◆◆	Municipal	High	764.7	0.72	24.4	10.6	28.7	6.3	7.1	22.7		–6.5– –12.2	–8.6
ERCAPITAL QUAL. MUNI. INVMT.	◆	Municipal	Average	386.9	0.74	20.4	10.7	22.8	5.8	7.4	25.1		–2.1– –7.7	–5.5
ERCAPITAL QUAL. MUNI. SEC.		Municipal		388.1	0.83	35.4	NA	27.0	NA	6.5	23.1		–10.7– –18.9	–14.8
ESTMENT GRADE MUNICIPAL	◆◆◆	Municipal	Very high	242.9	1.70	25.1	9.2	21.0	3.4	6.4	21.9		–9.7– –19.3	–14.9
IPER HIGH-INCOME	◆	Corp Hi Yld	Very low	202.5	1.64	16.7	11.1	24.2	10.3	9.7	8.1		8.9– –0.3	8.5
IPER INTERMEDEDIATE GOVT.	AVG	Government	Low	284.6	0.94	17.5	6.7	12.3	2.4	8.2	7.9		–5.8– –14.1	–8.8
IPER MULTI-MARKET INCOME	◆◆	Multisector	Low	217.4	1.03	21.6	10.8	31.1	12.9	10.3	12.1		1.0– –9.6	–0.5
IPER MUNICIPAL INCOME	AVG	Municipal	Average	681.8	0.70	17.9	8.1	33.4	8.7	6.8	30.7		4.0– –6.3	5.5
NAGED HIGH INCOME		Corp Hi Yld		470.8	1.19	17.2	NA	21.3	NA	10.6	7.8		–1.2– –8.2	–3.4
NAGED MUNICIPALS	◆	Municipal	Average	428.0	1.02	20.2	9.3	28.9	9.7	6.2	23.5		–2.4– –10.0	–2.6
S CHARTER INCOME	◆	Multisector	Low	784.7	0.86	18.6	9.8	12.9	6.5	7.4	8.9		–8.3– –15.8	–12.4
S GOVERNMENT MARKETS INCOME	AVG	Multisector	Average	600.5	0.97	19.4	8.5	11.2	4.3	5.6	11.1		–7.9– –17.2	–12.7
S INTERMEDIATE INCOME	AVG	Multisector	Average	1200.0	0.91	19.0	8.9	16.3	5.3	6.9	6.6		–8.5– –17.9	–14.5
S MULTIMARKET INCOME	◆	Multisector	Average	781.6	1.14	20.3	9.6	14.9	5.8	6.8	10.0		–9.3– –16.7	–9.7
S MUNICIPAL INCOME	◆◆◆	Municipal	Very low	335.8	1.31	10.7	7.6	20.2	12.3	7.2	18.7		9.3– 2.4	11.1
NTGOMERY STREET INCOME SEC.	AVG	Corp General	Average	200.9	0.71	21.8	9.4	23.7	3.0	7.8	13.6		–2.0– –12.3	–4.2
RGAN STANLEY EMERG. MKTS. DEBT		International		266.3	2.30	26.2	NA	36.6	NA	13.7	18.3		7.6– –12.8	4.2

of 2/1/96. ** As of 1/31/96 NA Not available

DATA MORNINGSTAR, INC., CHICAGO, IL

	RATING	CATEGORY	RISK	SIZE	FEES	1995 RESULTS				PORTFOLIO		TREND	PREMIUM/DISCOU
				ASSETS	EXPENSE	NAV RET (%)		SHARES RET (%)		YIELD	MAT	3-YEAR	DIFFERENCE FROM NA
				$MIL.	RATIO (%)	1 YR	3 YRS	1 YR	3 YRS.	(%)	(YRS.)	ANALYSIS	1995 HIGH-LOW
MUNICIPAL INCOME	▲	Municipal	Low	316.6	0.65	14.1	6.6	10.9	2.5	6.5	20.2		–5.4– –13.6
MUNICIPAL PREMIUM INCOME	AVG	Municipal	Average	372.4	1.21	19.1	8.8	13.5	2.9	7.6	21.8		–1.7– –13.3
MUNIENHANCED	▼▼	Municipal	High	510.5	0.69	23.9	9.2	22.9	2.3	6.8	22.5		–5.4– –13.8
MUNIVEST	▼	Municipal	High	881.5	0.66	23.6	9.6	24.6	2.1	7.2	19.1		–5.3– –14.2
MUNIYIELD	▲	Municipal	Average	840.1	0.66	23.3	10.5	27.3	6.6	6.9	21.6		–5.8– –13.3
MUNIYIELD CA	▼	Municipal	High	381.9	0.66	24.9	10.2	23.4	5.1	6.7	18.7		–5.2– –15.3
MUNIYIELD CA INSURED	▼▼▼	Municipal	Very high	347.3	0.68	27.8	9.4	25.0	3.3	6.4	23.2		–4.8– –15.0
MUNIYIELD INSURED	▼	Municipal	High	1041.3	0.66	25.3	10.6	24.8	5.9	6.6	24.1		–7.8– –15.1
MUNIYIELD NJ	▼	Municipal	High	199.1	0.74	22.4	9.7	24.9	4.1	6.5	18.8		–7.4– –14.5
MUNIYIELD NY INSURED	▼	Municipal	High	279.3	0.70	24.4	9.8	25.8	5.9	6.2	22.4		–3.7– –12.5
MUNIYIELD QUALITY	▼	Municipal	High	659.4	0.66	25.2	10.3	20.5	5.2	7.0	23.0		–7.8– –16.4
NEW AMERICA HIGH-INCOME	▲▲▲	Corp Hi Yld	Low	264.8	0.89	28.1	17.1	33.4	19.9	11.4	8.3		9.0– –3.6
NUVEEN CA INVEST. QUAL. MUNI.	▲▲	Municipal	Low	300.9	0.81	18.4	8.3	21.2	7.0	6.5	21.8		1.9– –3.9
NUVEEN CA PERFORM PLUS MUNI.	▲▲	Municipal	Low	282.5	0.83	18.5	7.8	26.7	6.3	6.7	21.9		–0.2– –6.4
NUVEEN CA QUALITY INC. MUNI.	▲	Municipal	Average	471.9	0.80	23.4	10.0	31.1	8.7	6.4	20.8		–2.6– –9.7
NUVEEN CA SELECT QUAL. MUNI.	AVG	Municipal	Average	490.9	0.80	22.6	9.2	31.3	8.1	6.4	23.1		–0.8– –8.3
NUVEEN INSURED CA PREM. INC. 2		Municipal		259.5	0.84	32.3	NA	30.1	NA	6.2	22.4		–0.8– –12.7
NUVEEN INSURED MUNI. OPPORT.	AVG	Municipal	Average	1823.5	0.79	22.6	9.6	30.1	8.1	6.5	24.1		–1.5– –8.3
NUVEEN INSURED PREM. INC. 2		Municipal		420.4	0.83	32.7	NA	28.7	NA	6.3	21.7		–4.0– –15.3
NUVEEN INS. QUAL. MUNI.	▼	Municipal	Average	842.3	0.82	19.7	8.3	24.6	4.9	6.7	24.2		–0.9– –7.4
NUVEEN INVESTMENT QUAL. MUNI.	AVG	Municipal	Low	800.9	0.79	18.1	8.1	22.6	4.2	7.1	22.0		–0.5– –7.2
NUVEEN MUNICIPAL ADVANTAGE	▲	Municipal	Low	948.7	0.79	18.0	8.3	28.7	6.2	6.8	22.9		0.3– –6.1
NUVEEN MUNICIPAL MARKET OPP.	▲	Municipal	Low	1000.1	0.78	18.0	8.1	28.7	6.5	6.8	21.9		–0.9– –6.8
NUVEEN MUNICIPAL VALUE	▲▲	Municipal	Very low	1994.4	0.70	14.0	6.7	13.3	2.8	6.5	21.3		2.0– –7.8
NUVEEN NJ PREMIUM INC. MUNI.	▼▼▼	Municipal	High	260.2	0.94	25.5	8.2	26.7	1.6	6.1	18.6		–4.5– –12.6
NUVEEN NY INVEST QUAL. MUNI.	AVG	Municipal	Average	396.0	0.84	16.5	7.9	28.1	7.2	6.3	24.4		4.5– –3.8
NUVEEN NY PERFORM PLUS MUNI.	▲▲▲	Municipal	Low	340.2	0.86	16.1	9.0	24.3	8.3	6.6	23.3		3.5– –5.7
NUVEEN NY QUALITY INC. MUNI.	▼	Municipal	Average	528.0	0.81	21.0	9.1	31.1	9.5	6.0	23.6		–2.0– –7.8
NUVEEN NY SELECT QUAL. MUNI.	▲	Municipal	Average	505.3	0.82	18.7	9.1	32.2	9.9	6.2	22.7		0.4– –6.0
NUVEEN PA PREMIUM INC. MUNI. 2		Municipal		329.7	0.92	30.2	NA	24.2	NA	6.5	21.2		–1.8– –14.5
NUVEEN PERFORMANCE PLUS MUNI.	▲▲	Municipal	Low	1285.1	0.79	15.3	7.6	29.1	7.8	6.9	22.6		1.7– –4.6
NUVEEN PREMIER INSURED MUNI.	▼	Municipal	Average	434.3	0.81	22.2	10.0	26.1	8.4	6.4	21.9		–1.7– –9.8
NUVEEN PREMIER MUNI. INCOME	▲	Municipal	Average	438.9	0.81	20.1	10.0	31.6	9.7	7.1	20.0		–1.1– –8.3
NUVEEN PREMIUM INCOME MUNI.	AVG	Municipal	Low	1306.0	0.77	17.9	7.0	20.3	3.0	7.2	23.6		1.2– –6.8
NUVEEN PREMIUM INCOME MUNI. 4		Municipal		865.6	0.88	27.9	NA	29.4	NA	6.7	20.0		–7.0– –15.5
NUVEEN QUALITY INCOME MUNI.	AVG	Municipal	Average	1211.4	0.79	20.0	8.9	28.7	8.1	6.9	22.8		–0.8– –6.8
NUVEEN SELECT QUALITY MUNI.	AVG	Municipal	Average	744.9	0.80	19.6	8.2	23.6	5.7	7.0	22.3		0.3– –6.6
NUVEEN SELECT TAX-FREE INC. 2	AVG	Municipal	Low	261.1	0.41	17.5	8.4	23.9	10.3	6.0	20.6		0.0– –6.7
OPPENHEIMER MULTI-SECTOR INC.	▲	Multisector	Average	294.5	1.02	15.3	9.4	10.0	5.8	9.9	9.7		3.4– –7.3
PILGRIM PRIME RATE	▲	Corp General	Very low	867.8	1.30	7.9	7.6	15.5	8.9	10.1	5.5		–2.4– –15.8
PUTNAM HIGH YIELD MUNICIPAL	▲▲	Municipal	Low	240.2	1.17	16.1	8.1	23.4	6.7	7.4	23.5		11.4– 1.6
PUTNAM INTERMED GOVT. INCOME	AVG	Multisector	Average	556.2	0.87	18.3	7.7	15.8	4.1	7.9	9.2		–7.4– –14.0
PUTNAM INVEST GRADE MUNI.	AVG	Municipal	Average	383.3	1.45	17.0	8.1	23.5	9.3	7.1	24.4		12.1– 4.2
PUTNAM MANAGED MUNI. INCOME	▲	Municipal	Average	624.5	1.20	18.8	9.0	23.2	8.8	7.0	23.2		6.6– 0.2
PUTNAM MASTER INCOME	▲▲	Multisector	Low	479.4	1.02	19.8	10.1	18.2	6.3	8.6	9.9		–6.0– –14.0
PUTNAM MASTER INTERM. INCOME	▲	Multisector	Low	326.9	1.03	19.0	9.3	21.0	6.6	8.3	7.5		–8.3– –14.0
PUTNAM MUNI OPPORTUNITIES		Municipal		257.6	0.95	21.9	NA	22.7	NA	7.4	26.0		1.2– –8.2
PUTNAM PREMIER INCOME	▲	Multisector	Low	1192.2	0.82	20.1	10.1	21.1	7.6	8.7	9.9		–5.9– –13.2
PUTNAM TAX-FREE HEALTH CARE	▲▲	Municipal	Low	194.5	0.90	14.9	8.5	6.5	4.5	7.7	21.8		1.1– –12.4
RCM STRATEGIC GLOBAL GOVT.		Multisector		356.1	1.15	17.0	NA	12.6	NA	8.1	7.4		–7.9– –14.6
SALOMON BROS. 2008 WORLDWIDE		International		271.4	1.01	35.6	NA	28.3	NA	11.1	18.7		13.5– –7.4
SELIGMAN SELECT MUNICIPAL	AVG	Municipal	Average	235.3	0.90	17.1	8.2	28.6	7.3	6.7	23.2		2.1– –6.2
SENIOR HIGH-INCOME		Corp Hi Yld		231.1	2.46	15.4	NA	18.3	NA	10.9	6.4		3.5– –8.8
STRATEGIC GLOBAL INCOME	AVG	International	High	285.2	1.27	19.7	10.0	16.5	7.2	9.4	12.9		–13.6– –20.0
TCW CONVERTIBLE SECURITIES	AVG	Convertible	Average	264.6	0.79	23.4	11.5	33.4	12.9	4.0	8.9		12.4– –0.5
TCW/DW TERM 2000		Government		496.1	3.25	36.9	NA	15.3	NA	5.5	14.3		2.7– –17.4
TCW/DW TERM 2002	▼▼	Government	High	460.8	3.08	40.5	9.2	6.7	0.9	7.6	17.5		12.1– –17.3
TCW/DW TERM 2003		Government		992.6	3.18	39.7	NA	17.3	NA	7.1	14.7		–1.0– –18.6
TEMPLETON EMERG. MKTS. INCOME		International		563.2	0.81	18.7	NA	24.6	NA	11.2	9.8		5.0– –7.6
TEMPLETON GLOBAL INCOME	AVG	International	Average	1007.0	0.78	19.6	10.0	18.8	0.4	10.0	8.4		–11.4– –17.8
VAN KAMPEN AM. CAP. ADV. MUNI.	▼▼▼	Municipal	Very high	499.5	1.64	25.2	9.0	23.1	8.1	7.0	22.2		–2.8– –10.4
VAN KAMPEN AM. CAP. BOND	AVG	Corp General	Average	233.7	1.50	23.9	10.5	26.9	6.8	7.9	20.1		–4.3– –10.6
VAN KAMPEN AM. CAP. CA QUALITY	AVG	Municipal	Average	228.4	1.66	26.0	9.8	29.3	9.5	6.8	23.9		–2.4– –9.4
VAN KAMPEN AM. CAP. MUNI.	▼▼	Municipal	High	871.8	1.65	22.9	8.6	16.8	3.8	7.5	20.4		–3.7– –14.7
VAN KAMPEN AM. CAP. MUNI. INCOME	▼▼	Municipal	Average	450.6	1.33	18.4	6.6	16.3	3.3	7.8	18.2		16.7– 2.5
VAN KAMPEN AM. CAP. MUNI. OPPORT.	▼▼▼	Municipal	Very high	387.7	1.69	24.8	9.3	13.7	3.4	7.4	21.1		–5.0– –18.8
VAN KAMPEN AM. CAP. STRAT. SECT.		Municipal		241.4	1.61	24.1	NA	18.4	NA	7.1	21.6		–5.7– –17.0
VAN KAMPEN AM. CAP. TR. INS. MUNI.	▼▼	Municipal	High	246.6	1.57	23.6	9.4	29.2	9.5	6.6	22.8		–2.3– –7.6
VAN KAMPEN AM. CAP. TR. INV. GR. MUNI.	▼	Municipal	High	701.5	1.63	24.2	9.9	23.3	8.4	7.2	23.7		–2.1– –8.7
VAN KAMPEN AM. CAP. VALUE MUNI.		Municipal		556.6	1.70	25.4	NA	22.1	NA	7.3	21.4		–8.2– –16.4

* As of 2/1/96. ** As of 1/31/96. NA = Not available.

DATA: MORNINGSTAR, INC., CHICAGO

"Thanks to Sprint Business, we're doing more business in skis."

— Hank Kashiwa, Olympic Skier
Co-founder, Volant Skis

"We make state-of-the-art skis. But the way we sold them was outdated."

Volant is a young, fast-growing company with global ambitions. But their communications system wasn't helping them realize their full potential.

"Sprint came in and showed us which technology was right for us."

Sprint consultants did an extensive analysis of Volant's business. And came up with real solutions for them — like putting inventory on-line for real-time access. And videoconferencing — to present new products worldwide.

"Now we're doing business a whole new way."

Today Volant is a more nimble, more profitable company. Because Sprint made their communications as cutting-edge as their stainless steel skis. Call us. We can help your business do more business, too.

Sprint®

We Help Business
Do More Business

1•800•816•REAL

Real BUSINESS	Real PROBLEM	Real SOLUTION	Real RESULTS
Volant Skis	Outdated field sales communications	Instant access to inventory data	Faster shipping, reduced inventory risk

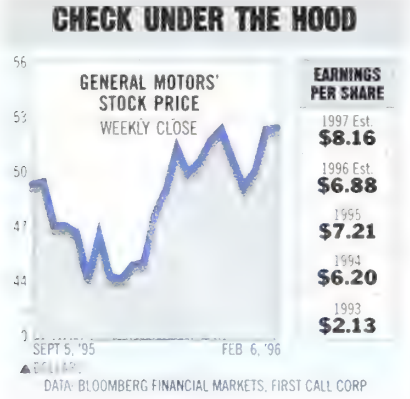
BY GENE G. MARCIAL

VROOM! VROOM! AT GENERAL MOTORS

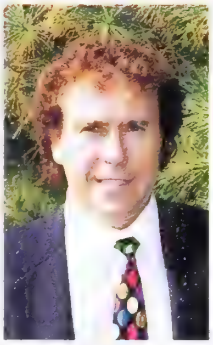
General Motors (GM) has been putting the pedal to the metal: Its shares hit a high of 54¾ on Jan. 30 after the auto giant reported 1995 record earnings of $6.9 billion and boosted the quarterly dividend 33%, to 40¢ a share. Some analysts caution that the stock may have already peaked—it edged down to 52½ on Feb. 6. But other money pros don't think so.

"Not by a long shot," insists investment manager Bob Olstein, who values companies purely on the quality of their earnings strength and capacity to produce excess cash flow. "Based alone on the value of GM's major assets—excluding Electronic Data Systems, which GM has decided to spin off—the stock is worth 83 a share," figures Olstein, who heads the $100 million Olstein Financial Alert Fund in White Plains, N. Y.

Olstein says the market has yet to focus on the carmaker "as a great value investment" and recognize the "significant improvement in GM's balance sheet, excess cash flow, and brilliant cost-cutting program" over the past three years. Excess cash flow is cash derived from operations after payment of all capital expenditures. "Under CEO John F. Smith Jr.'s leadership," says Olstein, "GM has been transformed into a cash machine, generating excess cash flow of $4.5 billion a year."



Olstein is convinced that management will strive to close the gap between the stock's current price of 53 and its estimated private market value of 83. "If it doesn't, GM could well attract a leveraged buyout group that could take it private." Olstein notes that "a KKR group or the likes of a Kirk Kerkorian could go for a GM LBO."


OLSTEIN: *Believes GM's real value is 83 a share*

According to Olstein, GM's auto and finance operations are worth $42 billion, or 56 a share. Its Hughes Electronics subsidiary, including its DirecTV unit, is worth at least 27, he estimates. GM Hughes, a worldwide leader in satellite communications—in which AT&T has invested $137.5 million for a 2.5% equity stake—is "GM's real hidden gem." The Street doesn't realize, Olstein says, that GM owns 100% of Hughes and often forgets that GMH shareholders only have a right to Hughes's dividend, equal to 35% of Hughes's earnings, and the right to receive a 20% premium in the auto maker's stock if GM decides to sell Hughes or buy in its shares.

"But the real play is in GM shares—not GMH," he argues, "because it isn't in the interest of GM to buy back the GMH shares." The parent only pays out 35% of GM Hughes's earnings to GMH shareholders ($88 million) and retains about $1 billion in aftertax earnings, explains Olstein. An investor who wants a direct play on satellite communications or DirecTV, and at the same time the chance to participate in GM's huge excess cash flow, "should own GM shares," he says.

AN ALTERNATIVE TO HYSTERECTOMIES?

There's an underserved market in health care: Women with severe gynecological problems. Investment pro Sam Navarro of UBS Securities says that Gynecare (GYNE) is one of the few new companies attempting to serve that market. Specifically, the company is using innovative technology to treat uterine disorders. Its first product is a device that helps stop excessive menstrual bleeding, a problem that affects at least 18 million women worldwide, Navarro notes.

The Gynecare device, which goes under the name Uterine Balloon Therapy, is designed as a one-time outpatient treatment. High temperature e ables the removal of the endometr lining of the uterus, the primary sour of menstrual bleeding, through a pa ented method called thermal ablatio

A balloon catheter is inserted in the uterus. It is then inflated with small amount of sterile fluid to co form to the shape of the uterus. heating element inside the balloon ra es the temperature to about 87 d grees Celsius, which is maintained f eight minutes. The balloon then d flates and the catheter is removed the endometrial lining is taken out.

Navarro notes that about 300,0 hysterectomies are performed worl wide each year because of heavy blee ing. Gynecare has started clinical tes of the therapy, which serves as an a ternative to hysterectomies, at 13 ac demic and medical centers in the U.

Navarro thinks the stock, trading around 9, remains undervalued and worth twice that, considering the p tential sales of the device. He se Gynecare making money in two yea

HONK IF YOU NEED EXTRA COVERAGE

In the fiercely competitive auto insu ance business, the small operator a pears doomed to extinction. But so f tiny Automobile Protection Co. (APC is alive and thriving. In fact, earnin rocketed 121% and revenues zoom 58% in 1995's fourth quarter. For all last year, APCO's profits jumped 44%, $1.5 million, or 20¢ a share; revenu climbed 65%, to $49.2 million. APC stock, which traded at around 2½ mid-December, has climbed to 3¼.

What's firing up APCO? The low-c packager of insurance to auto deale nationwide has a growing core bu ness, EasyCare. It offers extende service warranties, a business don nated by the Big Three auto make APCO's credibility was bolstered wh Honda Motor signed a five-year co tract to provide extended warran service to Honda and Acura deale in the U. S.

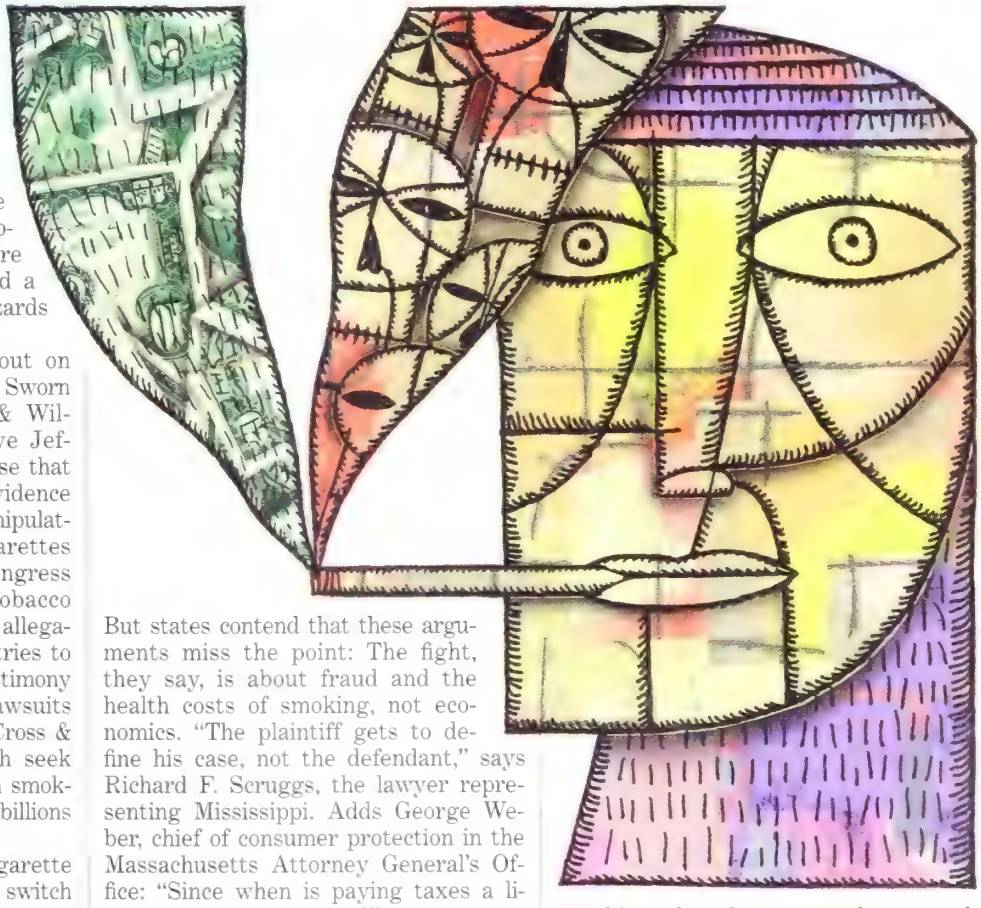
Herbert Davidson, an analyst Meyer Pollock Robbins in McLean, V says the stock should rise anywhe from 6 to 8 a share in a year. APC tiny size, he adds, led by an aggressi management that's fast to respond dealers' warranty needs, has enabled to carve a comfortable niche in the billion warranty business.

KING

OES TOBACCO AY ITS WAY?

ting tactics, the industry asserts that excise taxes offset any health costs to states

ew industries have been more adept than tobacco at snuffing out claims that its products are dangerous. re than two decades of le- ussles, cigarette makers racked up an enviable l by insisting on a simple smokers know the risks asso- with smoking and therefore argue they innocently used a ct, only to learn of its hazards



w, time may be running out on bacco's favorite arguments. Sworn nents by former Brown & Wil- on Tobacco Corp. executive Jef- . Wigand make a strong case that o companies covered up evidence icotine is addictive and manipulat- e level of nicotine in cigarettes hat executives lied to Congress what they knew. The tobacco anies vehemently deny the allega- But even as the industry tries to dit Wigand, it's clear his testimony become a cornerstone of lawsuits ht by five states and Blue Cross & Shield of Minnesota, which seek over more than $5 billion in smok- lated health-care costs and billions in punitive damages.

ing these tough attacks, cigarette 's are desperately trying to switch fields. In the case brought by Mis- pi, where Wigand's testimony first to light, tobacco industry lawyers laid the ground for a defense on the economics of tobacco. The tactic—also expected in lawsuits orida, Massachusetts, Minnesota, West Virginia—has three main : States already are compensated okers' health costs by the revenue hefty excise taxes. Smoking im- little extra cost on local govern- —and may even save states mon- hen sick people die young. And, health costs cannot fairly be sep- l from Big Tobacco's overall contri- n to a state's economy.

a nifty tactical shift by tobacco. But states contend that these arguments miss the point: The fight, they say, is about fraud and the health costs of smoking, not economics. "The plaintiff gets to define his case, not the defendant," says Richard F. Scruggs, the lawyer representing Mississippi. Adds George Weber, chief of consumer protection in the Massachusetts Attorney General's Office: "Since when is paying taxes a license to violate the law?"

A body of new studies and a review of state economic trends may give the states ammunition against tobacco's new line of defense. A report released in late January by the Centers for Disease Control finds the direct medical cost of smoking totals $50 billion a year nationwide, more than double the $21 billion in revenue from tobacco agriculture and manufacturing.

A soon-to-be-released study by two University of Michigan professors is expected to conclude that tobacco accounts for a net economic loss in all but six big tobacco-growing states and that states would gain substantially if people spent their cigarette money on nearly anything else, from pretzels to stock portfolios. "Fifty cents of every dollar [spent on cigarettes] is exported to North Carolina and the other tobacco states, and only half remains to benefit the local economy," says Kenneth E. Warner, one of the study's authors.

DUELING ECONOMISTS. Tobacco lawyers will scramble to muster whatever data they can find, including government research, to counter the mounting evidence that tobacco is a net economic drain. Cigarette manufacturers argue that taxes are already paying for any economic costs that tobacco imposes. In 1993, tobacco sales accounted for $13 billion in federal, state, and local tax revenue, more than four times the

$3 billion value of the crop that year.

A report by the Office of Technology Assessment found that smokers in 1993 paid $13.3 billion in excise and sales taxes but cost governments only $8.9 billion in health-care expenses. And the Tobacco Institute, the industry-funded advocate, is expected to release a report within weeks claiming that tobacco has a positive economic impact on the U.S. through job creation, exports, marketing, and capital spending. The study will deny that smoking creates significant net health costs, sources say.

DOUBLE-DIPPING? These figures, say industry lawyers, don't even take into account other contributions cigarette manufacturers make by creating retail jobs and buying billboard space, for instance. Advertising expenditures run $6.2 billion a year, and tobacco lawyers and lobbyists rack up untold millions in fees each year defending the golden leaf from its legions of adversaries. "There are significant supporting numbers to say that we're a net plus" to many states, says Thomas F. McKim, R.J. Reynolds Tobacco Co. counsel for tobacco litigation.

The industry plans to argue that demands from states for further payment from Big Tobacco amount to double-dipping. Legally, they contend, states cannot claim financial harm if they fail to establish that smoking causes uncompensated damage. "It's basically inconsistent for the states to say, on the one hand, we want the benefit of excise taxes, but on the other hand, we want reimbursement for health care," explains Daniel W. Donahue, general counsel to R.J. Reynolds.

Nor are cigarette makers squeamish about making an even more controversial point in their defense. In cases pending in Minnesota and Mississippi, the industry's lawyers insist that Big Tobacco should be credited for reducing government spending on such items as Medicaid and Social Security as a result of the premature death of smoking victims. "It's the euthanasia defense," retorts Northeastern University law professor Richard A. Daynard, a leading anti-tobacco activist. "We've done everybody a great favor by killing these people off who would otherwise be receiving pensions."

Disparagement aside, the industry maintains that states are trying to saddle it with health-care costs unrelated to smoking. To prove the point, tobacco companies have obtained court approval to conduct case histories on about 20 people from Minnesota's so-called victim pool. The idea is to find out whether individuals have other ailments that may have caused their health problems, rather than blame tobacco entirely. "On a lifetime basis, smokers may cost the state no more than nonsmokers," says American Tobacco Co. lawyer Murray Garnick.

Trying to convince judges and juries that tobacco companies give more than they take is a bold gambit, particularly given the waning impact of tobacco on state and local economies. Despite near-record corporate profits, employment in tobacco farming and manufacturing is declining. The industry provides 700,000 production, manufacturing, and retail jobs, according to its own figures. Overall, however, output from the nation's 124,000 tobacco farms has been flat since 1990, at about 1.6 billion pounds, 25% below the level in 1975. Farmers planted only 674 million acres of tobacco last year, down 10% from 1993. And despite growth in overseas sales of tobacco products, Agriculture Dept. statistics show cigarette consumption in the U.S. has not climbed year-over-year since 1973.

To appreciate how far the clout of cigarette makers has fallen, consider the state of North Carolina, the largest tobacco producer. Today, tobacco accounts for only 20% of North Carolina's farm income today, down from 60% in 1950. Tobacco production has dropped 30% since 1993, and acreage has shrunk 40% in the same time. Richard N. Apple, a fifth-generation tobacco farmer from Brown Summit, N.C., expects to be the last in his family to raise tobacco. He has a nursery business to supplement his tobacco income, but he doesn't want his children following him into the crop. "There's just too much stress in it today," says Apple.

"There's just too much stress in it today."

—TOBACCO GROWER RICHARD N. APPLE

Still, Big Tobacco keeps fighting hard on all fronts. In November, cigarette manufacturers filed a preemptive lawsuit in Texas challenging Attorney General Dan Morales' right to sue the industry to recover the state's share of health-care costs, estimated at $2 billion by a CDC study. Other states challenging states' authority to pursue such claims have been filed in Massachusetts and Maryland. The harder approach is making headway: Colorado Attorney General Gale Norton decided not to pursue suit, citing the prohibitive costs.

CONSTITUTIONAL ISSUE? Elsewhere tobacco states are coming to the industry's defense. South Carolina Attorney General Charles Condon, for instance, is mulling over a lawsuit claiming the Food & Drug Administration's proposed regulation of tobacco as a drug violates states' sovereignty and the commerce clause of the Constitution. Tobacco farming and manufacturing in South Carolina are together a $200 million-a-year industry.

With so many states, not just individual smokers, now entering the fray, the personal responsibility issue may arise in a new way. Plaintiffs hope to persuade jurors that the argument the industry has always made—smokers know about cigarettes' health risks—should apply to tobacco companies. The goal is to take the principle of responsibility that the industry has been basing about and apply it to the industry itself," says Laurence H. Tribe, a Harvard Law School professor who is working pro bono on behalf of Mississippi, Florida, and Massachusetts. "The tobacco they've paid are not enough compensation for the harm done." That will now be up to judges and juries to decide.

By David Greising in Atlanta with Linda Himelstein in San Francisco with John Carey in Washington and Lori Bongiorno in New York

STATES TO TOBACCO: HERE'S THE BILL

STATE	ANNUAL STATE SPENDING ON SMOKING-RELATED HEALTH CARE (MILLIONS)
FLORIDA	$250
MASSACHUSETTS	240
MINNESOTA	350
MISSISSIPPI	200
WEST VIRGINIA	500

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arch and development to build the
reliable
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EDITED BY AMY DUNKIN

MACHINES YOU CAN TAKE TO HEART

SPORTS EQUIPMENT

We're the quirky civilization that rides elevators to the second floor and buys electronic stair steppers to condition our thighs. We drive to convenience stores and hurry back to our treadmills. Yes, we rely on machines to save us from working, then buy other machines to save our bodies from terminal flab. It's a roundabout way of staying in shape, and it's certainly not cheap. But if you want to get a good workout in front of the tube, an exercise machine may be the ticket.

There are plenty of marvels out there to work your pecs, quads, abs, and glutes. All you need are several hundred to several thousand dollars. The ultimate focus is the most important muscle of all, the heart. Today's machines come with all sorts of snazzy panel displays that make heart-watching easier than ever. But one warning before you start: An estimated 50% of the machines people buy sit idle in garages and spare bedrooms, abandoned after an initial burst of energy. So before you spring for one, get a doctor's O. K. and make sure you're ready to revamp your life to make room for this new routine.

Next, see which equipment works best for you. After all, when you put down the money, you're committing yourself, in theory, to thousands of hours on this machine, perhaps tens of millions of steps, oar-strokes, or revolutions. It had better be a motion your body likes.

Most fitness machines replicate common real-world forms of exercise, from rowing to riding a bike to walking. But for those who yearn for something entirely new, there's the rider. Pioneered by HealthRider—and now imitated by many others, including NordicTrack—the rider is a seat with handlebars on which you pull yourself up and down, almost like a cowboy on the very tamest of mechanical bulls.

Rider sales have rocketed, growing from zero to 27% of unit sales in the $3 billion fitness market in the past four years. The reason: A rider is particularly well-suited to exercise novices. The up-and-down motion gently works the chest, stomach, shoulders, and legs while you're sitting. They're also relatively cheap. While the HealthRider sells for $499, including extra weights, the company sells versions for as little as $199. The Nordicrider, featuring a handlebar that pushes and pulls, costs $299.

Riders are affordable, in part, because they don't have motors. Exercisers on a budget would do well to stick to motorless appara es, including rowers and machines, that cost well der $1,000. If you have heart set on a motor treadmill or stair-clim be ready to fork at least $1,500. Ot wise, you're likely to up with a rickety chine and an unde motor that won't s up to millions of steps, especiall you're heavy.

Treadmills are most popular c exercise mach with 42% of market. They well for a si reason: Most mans know to walk. Cadillacs of category are duced by Tr and start $3,500. Trotters powerful motors, sm cushioned belts that are on the joints, state-of-th monitors, and ironclad g antees. If you're looking similar features at a l price, consider the True It boasts a 2-horsepower tor and a large walking face and lists for $2,795.

Of course, treadmilling like jogging, exercise only the bottom half o body, unless you c weights and swing arms. But because the of aerobic exercise is t the heart into a ta range—a ballpark figu 220 beats per minute mi person's age—working big muscles

HEART MONITORS
$100-$200
The Polar F4 watch beeps when you go above or below your target heart rate

TREADMILLS
$1,500-$4,500
Treadmills are the most popular of exercise machines, with 42% of the fitness market

ROWERS
$400-$725
Consumers' worry about back injuries has reduced rowers' share of the market

ıe waist on a treadmill
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tionary bikes, which fo-
ın the same muscles,
several advantages over
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ting, they place less
on the ankles, knees,
ips. They also average
half the price. The lat-
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where you sit in what
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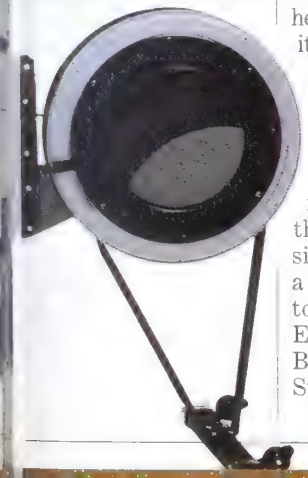
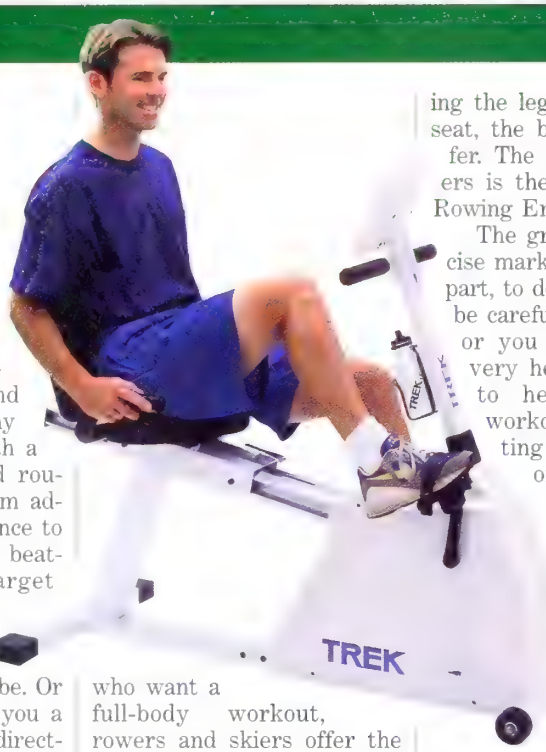


STATIONARY BIKES
$700-$1,500

Recumbent bikes, like the Trek R2200, are the latest rage because they are easy on the back and knees



HRT-1000R recumbent goes for $1,300 and offers smooth riding and slick controls. Like many machines, it comes with a set of preprogrammed routines. Its heart program adjusts the resistance to keep your heart beating at its target speed. The bike comes with a monitor that clips onto your earlobe. Or $100 more will get you a wireless connection directly from your chest. For $300 less, you can buy a Trek R2200 with many of the same features, minus the heart monitor. Both bikes simulate hills with magnetic resistance, which keeps noise, as well as wear and tear, to a minimum.

RIDERS
$200-$500

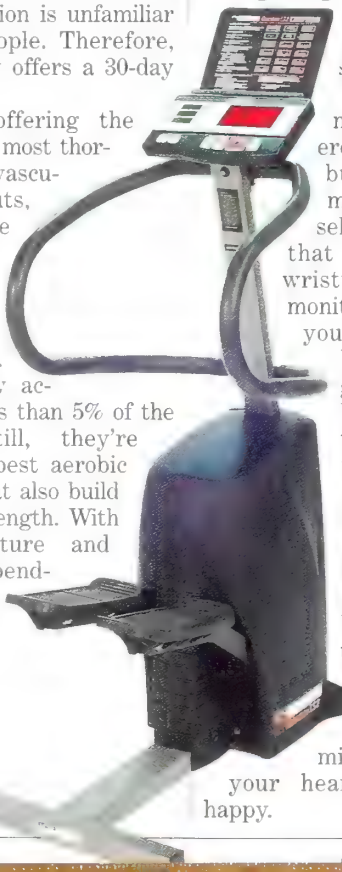
Riders are so quiet they actually bill themselves as the perfect machine for TV watching

The third option for the lower body is a stair-climber. "They're excellent for taking stress off the knees and hips," says Fredrick Hagerman, an exercise physiologist at Ohio University. Like a number of top-of-the-line machines, Bodyguard's Quantum LS series, starting at $1,899, keeps you within your target heart range. You wear a monitor around your chest, and the rate is fed to the machine, which adjusts its resistance to keep you on target. Bodyguard's climbers also feature a series of programs that allow you to simulate climbing a host of famous towers—from the Empire State Building to the Statue of Liberty.

For exercisers who want a full-body workout, rowers and skiers offer the most promise. NordicTrack's sturdy cross-country ski machines start at $299. Its Achiever, at $699, features more stylish oak, along with a few options, such as a hill simulation, heart monitor, and a wider, more stable frame. The cardiovascular workout of a ski machine is excellent. But the motion is unfamiliar to many people. Therefore, the company offers a 30-day tryout.

Despite offering the quickest and most thorough cardiovascular workouts, rowers have fallen into disfavor as consumers worry about their backs. Rowers now account for less than 5% of the market. Still, they're among the best aerobic machines that also build full-body strength. With proper posture and technique, bending the legs with the sliding seat, the back shouldn't suffer. The standard for rowers is the $725 Concept II Rowing Ergometer.

The growth in the exercise market is due, in large part, to doctors' orders. But be careful not to overdo it, or you risk hurting the very heart you're trying to help. Three good workouts a week, getting the heart to 70% of its target rate for 20 minutes, is the recommended minimum. Those who hold to the no-pain, no-gain adage, say the experts, are short on brain. "The trouble comes when people feel pain and they keep going," says Diane Markovitz, a physical therapist at Pittsburgh's West Penn/Harmarville Rehab Center. Her advice: Warm up for about five minutes on the machine. Then take time out to stretch before getting back on. If you feel sharp pain, slow down or stop.



Perhaps the most useful exercise aid you can buy is a heart monitor. Polar sells one for $100 that looks like a wristwatch. These monitors beep when you go above or below your target heart rate. You might want to use a monitor while out shoveling snow, walking to work, or climbing steps. Those activities, combined with regular turns on a rider, rower, stepper, or treadmill, should keep your heart and doctor happy. *Stephen Baker*

STEPPERS
$1,400-$2,300

The Quantum LS climber and other upscale models keep you within your target heart range

JUST RIGHT: *Henry-Griffitts fitter at Chelsea Piers*

TAILORED CLUBS COULD TRIM YOUR SCORE

If you're thinking of spending as much as $500 for one heavily advertised name-brand golf club, consider a cheaper, more personalized alternative: a custom-made club measured and fitted to your exact specifications. Extravagant? Not really. A customized club costs more than a basic model, but it can be far less expensive than best-selling brands such as Callaway's Great Big Bertha or the Taylor Made Burner Bubble.

SPORTS EQUIPMENT

Just how much of a difference can they make in your game? It depends on the quality of the fit and experience of the maker. Some fitters merely adjust the length of the shaft according to your height, while others take into account everything from swing speed to more esoteric indicators such as torque—how much the shaft twists during the swing. A properly fitted club makes it easier to hit the sweet spot without having to make compensations in your swing to find it. The real benefit is greater consistency and distance.

There are several ways to buy custom clubs. Of course, any pro shop can sell you off-the-rack clubs and make minor adjustments in the grip or shaft length, but this isn't customization. Still, "most people come into the shop predisposed to a brand rather than taking the time to go through a fitting," says Dave Alvarez, head pro at the new Chelsea Piers driving range in Manhattan.

RADAR GUN. Most of the major manufacturers offer their own fitting system that pros also may use. In the past two years, Slazenger Golf has abandoned its off-the-rack line to get into the custom-fitting business full-time. Rick Gomes, a teaching professional at Jonathan's Landing Golf Club in Jupiter, Fla., says his club chose the Slazenger system because it offers numerous variations of head and shaft weights and lie angle, which is the angle formed by the head of the golf club and the shaft.

The next level of customization is to get measured by a pro who will then order the components and assemble the clubs. Many pros do the measuring for free. Those who do charge typically bill the hourly lesson rate and then credit it toward a purchase. And if you can bring your own set of clubs, the fitter should be able to tell you how they fit. If you're looking for a qualified Professional Golfers' Assn. pro who does it all, you can call GolfSmith, a mail-order component company (800 933-4599), for a local referral.

Bill Ryan, an award-winning club fitter and maker, is one such pro. With a radar gun clocking my swing speed and a device assessing where in my swing I exert the most force, Ryan prescribed a slightly stiffer graphite shaft than the one I currently use. While two people might clock in on the radar gun at 90 mph at impact, they may well need shafts of differing flexibility. "The idea is not how fast you swing but how you swing fast," explains Kenneth Donovan, owner of the Garden State Golf Center in Somerville, N.J., where Ryan is head pro.

The advantage in worl with a professional is vice, and Henry-Griffitts ters—all PGA members—c bine technology with t own unique teaching proach. The company 445-GOLF), which ma nothing but custom cl takes the view that eq ment affects motion. "M people fear that if they nature take its course, th end up with a sloppy sw The reality is, nature provide you with a beau balanced swing if the fits," says Tom Shea, fitts regional director.

MIX AND MATCH. Shea me part of the reason I hitting poorly was that I compensating for an ill ting club. Doubtful, I fully hit 5-wood after 5-w from his hot-dog cart of tom clubs. Suddenly, it pened. Using a lighter, flexible 5-wood with a s er grip, I stopped pulling shots to the left and more distance than I got from my driver.

The least expensive to customization is to measured by a pro, take the specifications rectly to a club compo maker. This is comparab buying a computer a mail-order company ra than a retail store. Mu Flam, president of FM Sp in Brooklyn, N.Y. (718 3635), a clubmaker s 1946, has a wide variet shafts, heads, and grip his back room. He will the club to your specs fering a choice of parts can mix and match.

So before put down a hundred do for a King C driver in hopes that y start hitting Greg Nor keep in that you m be better o vesting in that will re your swing- his. *Kerry C*

Comparing Club Costs

MAKER	STEEL IRON	STEEL WOOD	GRAPHITE IRON	GRAPHITE WOOD
FM SPORTS Components maker	$24	$70	$35	$106
BILL RYAN Independent club fitter	40	75	60	159
KING COBRA National brand	62*	124*	99*	199*
SLAZENGER CROWN LTD. Specialty custom line	90	140	190	250
HENRY-GRIFFITTS Custom-club company	90	130	130	250

* Discount-store price.

DATA: COMPANY REPORTS

P-FLIGHT TRAIL BIKES, WN-TO-EARTH PRICES

ntain biking is kly becoming a t that requires a sary. "Screamers" eople who love cruising steep slopes. "Hard are bikes without a absorber built into the . "Table top" is the art ling the frame horizon- o the ground while ning air" off a jump. yone who dishes out lin- ch as that had better the wheels to back it check out some of the models, I spent an af- on riding these multi- d, shock-absorbing two- ers on the Olympic tain-biking course out- Atlanta. Together with edicated mountain bik- I tested a variety of —a "full suspension" Di- dback V-Link with a absorber in the frame, er Diamondback made ht carbon-fiber materi- ie by the well-known maker Klein Bicycles, couple of hard tails GT and Trek.

R "B's". The technology ountain biking has ad- d and the prices have ated enough that for $1,000, it's easy to find e with all the modern ities: front-wheel shock bers, an easy-shifting r setup, a lightweight , and dependable s—maybe even a full- nsion frame. Sure, that's money and more gear we used to spend on a that could handle the borhood newspaper But hitting the back- isn't kid's play, and I d to avoid the killer of mountain biking: a red behind, burning , and broken bones. eeded everything the could give and more to work my way through the Olympic course. This is the first year mountain biking is an Olympic sport, and the designers have built a course up to the challenge. The six-mile trail has a profile that looks like an electrocardiogram, weaving around and across the equestrian cross-country course at the Georgia International Horse Park in Conyers, Ga. There are steep uphill climbs and sharp downhills punctuated by surprise jumps; grueling long, steady inclines; and descents through tightly spaced trees. The circuit's signature feature: bone-jarring open runs across choppy granite outcroppings.

SPORTS EQUIPMENT

The best of the bikes we tested was the Diamondback WCF 6.0. This racy bike has a frame made of carbon fiber, which is extremely lightweight and sturdy—yet compliant enough to absorb bumps on the course's granite section. "The bike doesn't beat you up," says Chris Hovatter, a racer from the Cycleworks bike shop located outside of Atlanta. "Carbon fiber is definitely the material of the future." Although pricey—$1,600—the 24-pound WCF offers high-end componentry: a Manitou Mach 5 front shock absorber, Grip Shift's X-Ray gear shifters, and Ritchey clipless pedals. The same frame with lesser components can be had for $1,000. Its light weight makes it a good climber and quick accelerator.

LABELS FOR LESS. The Klein Pulse offers one extremely attractive element: the Klein frame, which features unique fat tubes of very thin aluminum and a sharply angled cross tube. Kleins typically cost $2,000-plus for the frame alone. But this bike is affordable— $1,100—because Klein has turned to quality Shimano parts for components such as the head set and bottom bracket, which are custom-made on higher-end models. "It may not have all the things that make a Klein a Klein, but the main thing is they're bringing the name down to a price where someone buying their first good mountain bike can afford it," says Elliott Hardin of Free-Flite bike shop in Marietta, Ga. The Klein was the best climber I rode, because its stiff frame transfers power directly to the drive train.

EASY RIDER: *Greising with the GT Ricochet*

The one full-suspension model I tried, Diamondback's $1,400 V-Link 3.0, offered an exceptionally smooth ride, thanks to the shock absorber under the seat. The V-Link is designed to eliminate the bobbing action that plagued earlier full-suspension bikes, but at 27 pounds, this version of the technology is heavy, making the bike a lug climbing hills. The Trek 8000 offers a sleek-looking bonded aluminum frame that's light but a little too stiff on the bumps. The Trek comes with standard handlebar ends that give an extra hand position for cruising and affords better leverage for climbing.

The GT Ricochet, the least expensive bike I tested at $790, offers the higher-end Shimano Allevia derailleurs, a small frame that handles well, and, at 26 pounds, a lightweight feel. The frame's compact geometry makes it especially good for cornering through tight twisting trails and also improves climbing efficiency. It's a good choice for someone who can't see making the $1,000 hurdle. But if you ever get on the Olympic bike course, that could well prove to be the easiest hurdle you'll have to handle. *David Greising*

A Sampling of Mountain Climbers

MODEL/PRICE	DESCRIPTION
DIAMONDBACK V-LINK 3.0 $1,400	Full suspension frame (built-in shock absorber); smooth ride, but heavy
DIAMONDBACK RACING WCF 6.0 $1,600	Light, strong carbon-fiber frame; responsive, speedy
GT RICOCHET $790	Compact design, good components, responsive turns, precise shifting
KLEIN PULSE $1,100	Unique high-end frame; best on steep climbs
TREK 8000 $1,100	Bonded aluminum frame; good climber

DATA: BUSINESS WEEK

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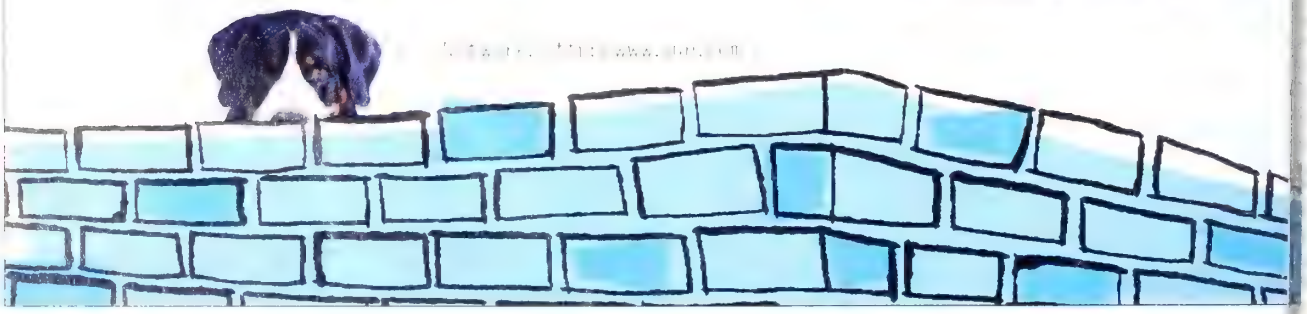

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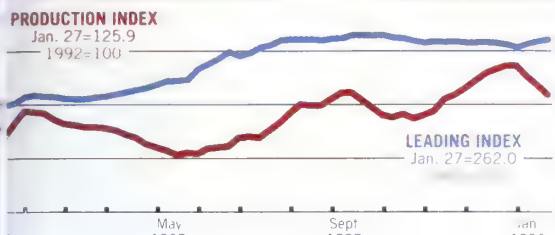

xes are 4-week moving averages

roduction index slipped again during the week ended Jan. 27. But calculation of the four-week moving average, the index edged up to , from 124.4, as the industrial sector shook off the problems caused by id-January blizzard. Auto and truck output rebounded in the latest week. **eading index** increased during the latest week, but the unaveraged index fell 0.6, from 262.3, dragged down by slower growth in real estate loans and M2.

DING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
K PRICES (2/2) S&P 500	632.94	616.96	34.1
ORATE BOND YIELD, Aaa (2/2)	6.82%	6.81%	-18.1
STRIAL MATERIALS PRICES (2/2)	109.8	110.2	-3.9
NESS FAILURES (1/26)	NA	NA	NA
ESTATE LOANS (1/24) billions	$505.8	$507.8r	9.0
Y SUPPLY, M2 (1/22) billions	$3,767.1	$3,774.9r	4.8
AL CLAIMS, UNEMPLOYMENT (1/20) thous.	413	316	25.5

es: Center for International Business Cycle Research (CIBCR), Standard & Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures e companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on ss failures and real estate loans

EREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
RAL FUNDS (2/6)	5.16%	5.37%	5.95%
IERCIAL PAPER (2/7) 3-month	5.16	5.31	6.14
IFICATES OF DEPOSIT (2/7) 3-month	5.16	5.24	6.16
MORTGAGE (2/2) 30-year	7.31	7.30	9.15
STABLE MORTGAGE (2/2) one-year	5.49	5.45	6.76
E (2/7)	8.25	8.25	9.00

es: Federal Reserve, HSH Associates, Reuters Holdings PLC

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (2/3) thous. of net tons	2,030	2,040#	-0.2
AUTOS (2/3) units	124,029	118,163r#	-10.2
TRUCKS (2/3) units	112,321	120,290r#	-6.1
ELECTRIC POWER (2/3) millions of kilowatt-hrs.	67,886	64,901#	10.6
CRUDE-OIL REFINING (2/3) thous. of bbl./day	13,636	13,697#	1.5
COAL (1/27) thous. of net tons	20,002#	19,616	-3.0
PAPERBOARD (1/27) thous. of tons	NA#	NA	NA
PAPER (1/27) thous. of tons	NA#	NA	NA
LUMBER (1/27) millions of ft.	449.0#	449.7	-5.8
RAIL FREIGHT (1/27) billions of ton-miles	24.4#	23.6	-2.4

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA[1], SFPA[2], Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (2/7) $/troy oz.	414.200	405.550	10.4
STEEL SCRAP (2/6) #1 heavy, $/ton	144.50	144.50	0.0
COPPER (2/3) ¢/lb.	121.1	121.3	-13.5
ALUMINUM (2/3) ¢/lb	73.5	73.0	-27.6
COTTON (2/3) strict low middling 1-1/16 in., ¢/lb	83.72	83.24	-6.5
OIL (2/6) $/bbl.	17.69	17.61	-4.0

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (2/7)	106.03	106.96	98.94
GERMAN MARK (2/7)	1.48	1.49	1.53
BRITISH POUND (2/7)	1.54	1.51	1.56
FRENCH FRANC (2/7)	5.08	5.11	5.29
ITALIAN LIRA (2/7)	1576.2	1597.0	1616.8
CANADIAN DOLLAR (2/7)	1.37	1.38	1.40
MEXICAN PESO (2/7)[3]	7.460	7.375	5.630

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

data in the production indicators are seasonally adjusted in computing the BW index (chart), other components (estimated and not listed) include machinery and defense ent. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

OYMENT COSTS

ay, Feb. 13, 8:30 a.m.EST ▶ Employ- costs for civilian workers probably 0.7% in the fourth quarter, accord- the median forecast of economists ed by MMS International, one of The w-Hill Companies. That would be faster than the 0.6% increase in rd quarter. For the year, labor costs be up just 2.6%.

LE GOODS ORDERS

lay, Feb. 15, 8:30 a.m.EST ▶ New for durable goods likely increased by n both November and December, rders fell 1.1% in October. To catch r the government shutdown, the Commerce Dept. will combine some economic reports for November and December into one release.

FACTORY INVENTORIES

Thursday, Feb. 15, 8:30 a.m.EST ▶ Manufacturing inventories probably increased by 0.4% in November and by only 0.1% in December. Factory stock levels grew by 0.4% in October.

CONSTRUCTION SPENDING

Friday, Feb. 16, 8:30 a.m.EST ▶ Outlays for building projects probably fell 0.5% in November and were flat in December, hurt by unseasonably cold weather. That follows a large 2.7% jump in October.

INDUSTRIAL PRODUCTION

Friday, Feb. 16, 9:15 a.m.EST ▶ Output at factories, mines, and utilities probably plunged 0.8% in January, says the MMS forecast. The blizzard caused massive plant closings, and factories have already reported a drop of 72,000 jobs. Output edged up 0.1% in December. Operating rates likely dropped to 82%, from 82.8%.

BUSINESS INVENTORIES

Friday, Feb. 16, 10 a.m.EST ▶ Inventories held at manufacturers, wholesalers, and retailers were little changed in November, on top of a 0.6% gain in October, says the MMS survey. Business sales probably rose 0.5%, after falling 0.4% in October.

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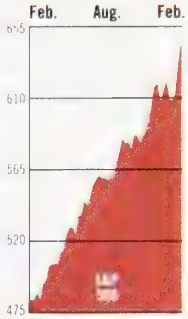
Business Week (ISSN 0007-7135) published weekly, except for one issue in January, by The McGraw-Hill Companies, Inc. Executive, Circulation, and Advertising Offices: 1221 Avenue of the Americas, New York, N.Y. 10020. U.S. subscriber rate $49.95/year; Can $69/year.Second-class postage paid at New York, N.Y., and at additional mailing offices. Postage paid at Montreal, P.Q. Canada Post Int Publications Mail Product Sales Agreement No. 246484 Postmaster: Send address changes to BUSINESS WEEK. P.O. Box 430, Hightstown, N

vestment Figures of the Week

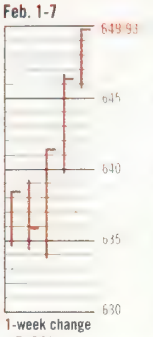
ENTARY

great week for stocks. The ndexes all posted new with the Dow industrials .8%. the S&P 500 2.2%, Nasdaq composite 2.4%. move in the Nasdaq re- a sharp rebound in comput- ts as well as continued n in biotech. But underlying the flood of money going market from mutual n January, investors poured f $24.5 billion into equity funds, topping the previous r high set two years ago by an $6 billion.

STOCKS

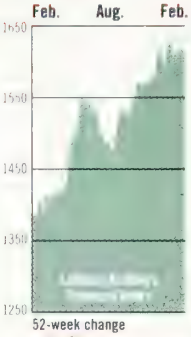


52-week change
+35.1%

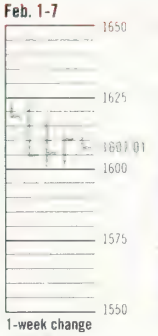


1-week change
+2.2%

BONDS

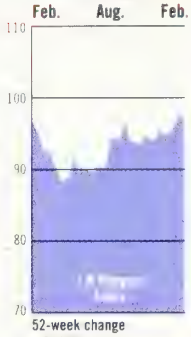


52-week change
+16.0%

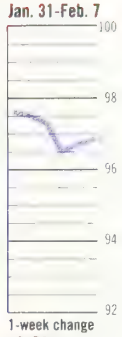


1-week change
-1.1%

THE DOLLAR



52-week change
+0.1%



1-week change
-0.8%

RKET ANALYSIS

OCKS	Latest	% change Week	% change 52-week
NES INDUSTRIALS	5492.1	1.8	39.6
E COMPANIES (S&P MidCap Index)	224.1	1.5	26.4
COMPANIES (Russell 2000)	319.4	1.3	25.9
MPANIES (Russell 3000)	369.0	2.0	33.9

GN STOCKS	Latest	% change (local currency) Week	52-week
(FINANCIAL TIMES 100)	3726.1	-0.9	21.3
NIKKEI INDEX)	20,943.5	0.6	14.5
0 (TSE COMPOSITE)	5026.5	1.2	22.5

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	4.94%	5.04%	5.89%
30-YEAR TREASURY BOND YIELD	6.15%	6.02%	7.64%
S&P 500 DIVIDEND YIELD	2.11%	2.14%	2.69%
S&P 500 PRICE/EARNINGS RATIO	18.8	18.1	16.4

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	574.3	571.0	Positive
Stocks above 200-day moving average	71.0%	70.0%r	Negative
Speculative sentiment: Put/call ratio	0.63	0.62 r	Neutral
Insider sentiment: Vickers sell/buy ratio	1.63	1.57	Positive

BLOOMBERG FINANCIAL MARKETS

USTRY GROUPS

ONTH LEADERS	% change 1-month	% change 12-month	Strongest stock in group	% change 1-month	% change 12-month	Price
ENSE ELECTRONICS	25.6	131.8	LORAL	28.3	124.8	46 1/2
PUTER SYSTEMS	20.0	50.6	DIGITAL EQUIPMENT	29.7	104.8	75 1/4
LS AND MOTELS	17.8	28.1	HILTON HOTELS	41.8	31.9	89 7/8
MUNICATIONS EQUIPMENT	15.9	60.3	TELLABS	25.3	83.4	47
) MINING	15.9	57.7	SANTA FE PACIFIC GOLD	28.8	98.6	17 7/8

ONTH LAGGARDS	% change 1-month	% change 12-month	Weakest stock in group	% change 1-month	% change 12-month	Price
HINE TOOLS	-10.7	-0.8	CINCINNATI MILACRON	-12.4	3.3	23 3/4
CKING	-7.6	-10.2	CONSOLIDATED FREIGHTWAYS	-15.1	10.1	23 1/4
UTION CONTROL	-4.6	-1.1	WMX TECHNOLOGIES	-6.1	0.0	29
EBUILDING	-4.4	30.5	CENTEX	-13.2	20.4	29 1/2
ERAL MERCHANDISE CHAINS	-4.3	1.8	KMART	-12.5	-49.6	7

TUAL FUNDS

MORNINGSTAR INC.

RS

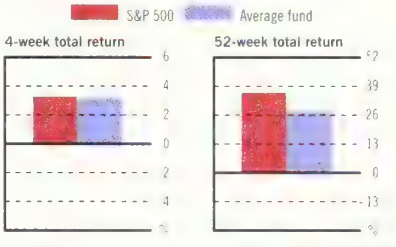
eek total return	%
AS	21.7
NCHARD PRECIOUS METALS	21.3
DDER GOLD	21.0

k total return	%
AS	106.0
ER CAPITAL APPRECIATION	80.5
PRECIOUS METALS A	79.8

LAGGARDS

Four-week total return	%
WRIGHT EQUIFUND-SWITZERLAND	-4.6
HOTCHKIS & WILEY SMALL CAP	-3.9
FIDELITY SELECT AIR TRANSPORTATION	-3.6

52-week total return	%
EV MARATHON GREATER INDIA	-29.2
AMERICAN HERITAGE	-25.9
STEADMAN AMERICAN INDUSTRY	-18.6



LATIVE PORTFOLIOS

DRI/McGRAW-HILL

amounts represent the t value of $10,000 d one year ago portfolio

tages indicate y total returns

U.S. stocks	Treasury bonds	Foreign stocks	Gold	Money market fund
$13,697	$12,767	$12,191	$10,583	$10,563
+2.57%	-1.16%	+1.94%	+1.43%	+0.12%

on this page are as of market close Wednesday, Feb. 7, 1996, unless otherwise indi- ndustry groups include S&P 500 companies only; performance and share prices are as of market close Feb. 6. Mutual fund returns are as of Feb. 2. Relative portfolios are valued as of Feb. 6. A more detailed explanation of this page is available on request. r=revised

THE BACKLASH BUILDING AGAINST BUSINESS

Is Corporate America in denial? When such nationalist conservatives as Presidential candidate Pat Buchanan and such militant labor leaders as new AFL-CIO President John J. Sweeney agree that corporations are the root cause of stagnant wages and downward mobility, something very serious is afoot in the land. So far, most Americans have tended to blame Big Government for their economic woes. But now their anger may be shifting in some measure toward Big Business. The role of the corporation in society is being challenged. Only the foolish would ignore the signs.

Who benefits from the new high-tech, global economy? That is the question both right and left are asking. Their answer is virtually identical: Despite big gains in productivity and profits, most employees are not sharing in the rewards, while shareholders and option-laden corporate officials most definitely are. The rising economic tide that once lifted everyone in America is now playing favorites, and people don't like the new rules. Cutting taxes can help, but it's not a real solution to families facing declining real income.

Buchanan's solution would be to go protectionist and halt immigration, stopping companies from freely trading and blocking the inflow of goods and people. That would curb competition and push up wages. Sweeney would up the minimum wage and also curb immigration and free trade. Not a pretty picture, if you're an executive intent on building a vibrant global enterprise.

New conservative and liberal philosophies also challenge the corporation's role in America. Reviving civil society is the motivating idea driving conservatives these days. Rebuilding the institutions of civil society—voluntary associations, churches, schools, and, of course, families—to replace inept government bureaucracies is their guiding light. But there is no way for that to happen without family income rising or parents getting more time off from work to raise their children and attend Boy Scout or PTA meetings. There is no way for civil society to be rebuilt unless businesses return to their tr[a]tional support of charities that look after their workers' w[e]ll being. Backing local hospitals and baseball teams are expe[n]ses delegitimized recently by shareholder pressure.

Voices from a reviving left are also calling for change[s] in the ways corporations operate. The motivating idea in lib[e]ral circles is to build a stakeholder society, which calls fo[r] a wider collection of corporate groups to join shareholders [in] checking chief executives in reaping the rewards of higher produ[c]tivity and profits. In Britain, the opposition Labor Pa[rty] leader Tony Blair is making this his clarion call to defeat [the] Conservatives. Just as civil society unites conservative [fac]tions—libertarians, religious conservatives, growth conse[r]vatives, and nationalists—under one principle, so, too, d[o] stakeholder society unite many liberal factions.

Whether building a civil or a stakeholder society, b[oth] right and left use the America of the second half of the [19]th and the early 20th century as their reference point. For g[ood] reason. It was an era of huge technological change, econo[mic] growth, and downward mobility. It was a time much like [our] own. Conservatives see it as a golden age of commun[ity] when the YMCA, libraries, and the Red Cross were created [of]ten with the patronage of industrialists. Liberals recall i[t as] the Progressive Era, when Populists were elected to b[ust] corporate trusts, establish fair labor laws, and set new rule[s] the game to protect working people in the marketplace.

What's clear is that both conservatives and liberals want [cor]porations to do more for society than boost their stock prices. [At] the recent World Economic Forum of top business and poli[tical] figures in Davos, Switzerland, the central theme was the gr[ow]ing backlash against the cold exigencies of global competi[tion]. CEOs would be wise to ponder these tectonic changes. [One] thing is certain: U.S. corporations may have to strike a [new] balance between the need to cut costs to be globally competi[tive] and the need to be more responsible corporate citizens.

BRING THE FREE MARKET TO CAR LOTS

We're always tickled to hear about arcane laws that promote monopoly and thwart competition in the interstices of America's otherwise free-market society. New York City has two of our all-time favorites: the rent stabilization laws that bar landlords from charging market rates for apartments, and the scheme that limits the number of yellow cabs on the streets to 11,787, the same number as in 1937. (O.K., so after hiking fares by 20%, New York will soon put 400 more cabs on the street. Thanks a lot.) We also really appreciate the American Medical Assn.'s recent call to limit the number of doctors in America because there were, by their measure, too many. Too many for what, we wonder.

The latest entry in our collection of America's Funniest Mo[st] nopolies is the auto dealer franchise law. There are dozen[s] these state laws that protect car dealers from competition, making it hard for national retailers to enter the new-car b[us]iness. Dealers, you should know, provide up to 20% o[f] state taxes in many states, as well as a big share of l[o]cal newspaper and TV advertising. They have political clout.

Consumers don't. Many, especially women, hate bu[ying] cars from smarmy, arrogant dealers and welcome the r[e]volution in selling cars through CarMax, AutoNation, an[d] whole new generation of national merchandisers. But [the] revolution is being slowed by those franchise laws. The st[ates] should take the advice Washington is fond of giving Ja[pan]. Open those markets to competition. Consumers will love [it].

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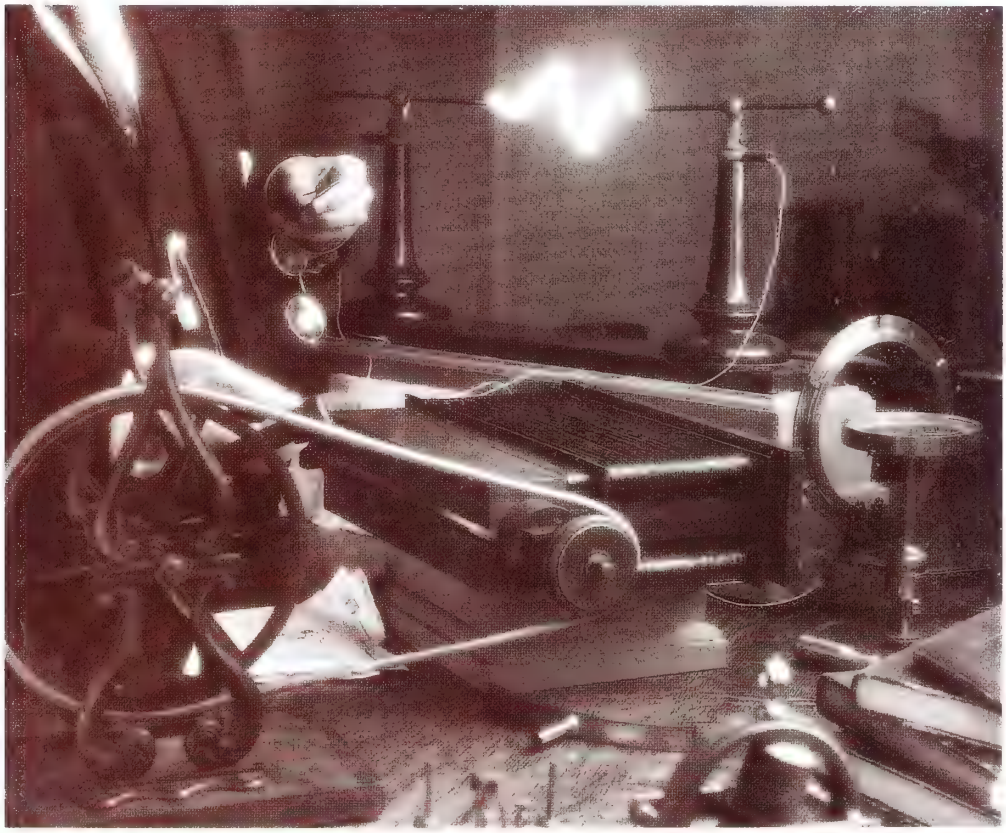

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SS WEEK
ebruary 26

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BusinessWeek

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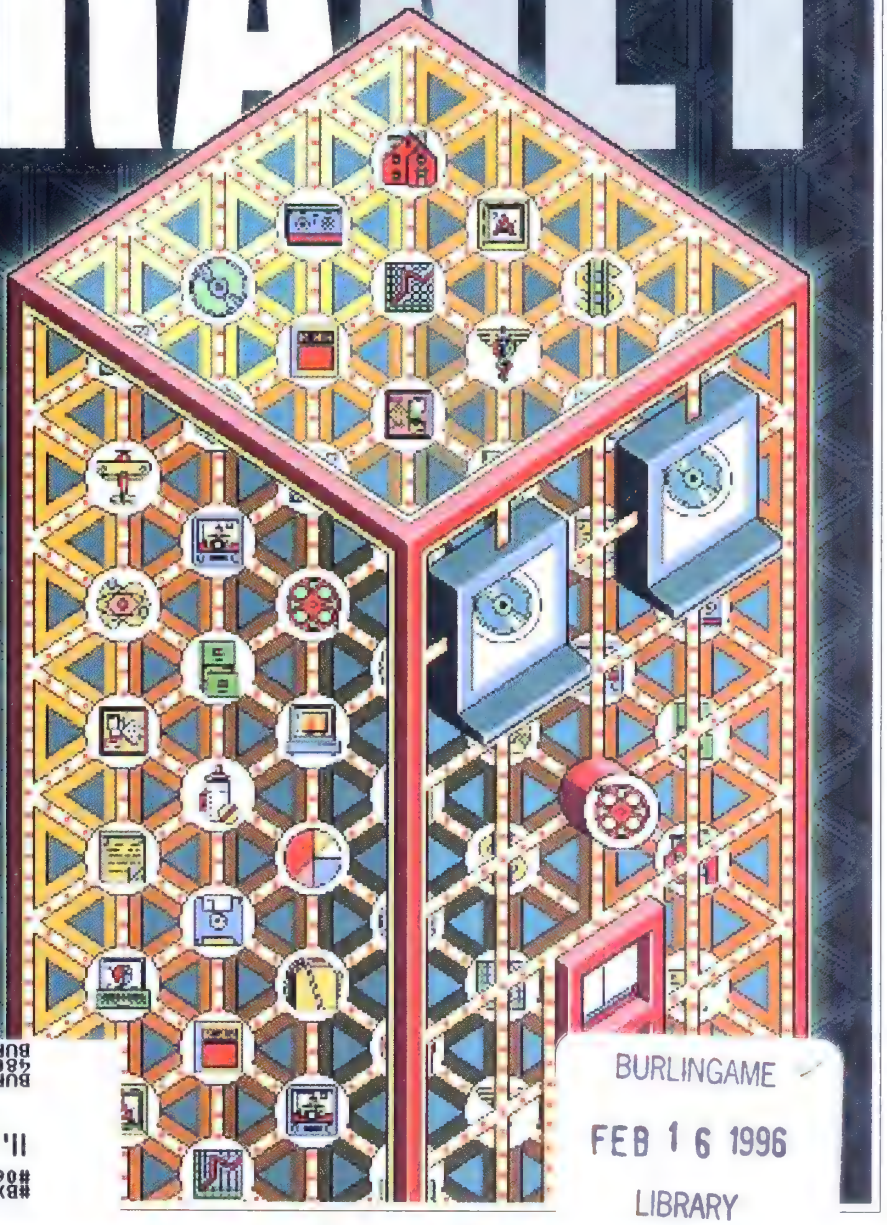
THE INTRANET

he Internet evolution has ome home – to nternal corporate etworks. Cheap, exible "intranets" re spreading verywhere – and ecoming a new anagement tool.

PECIAL REPORT

GE 76



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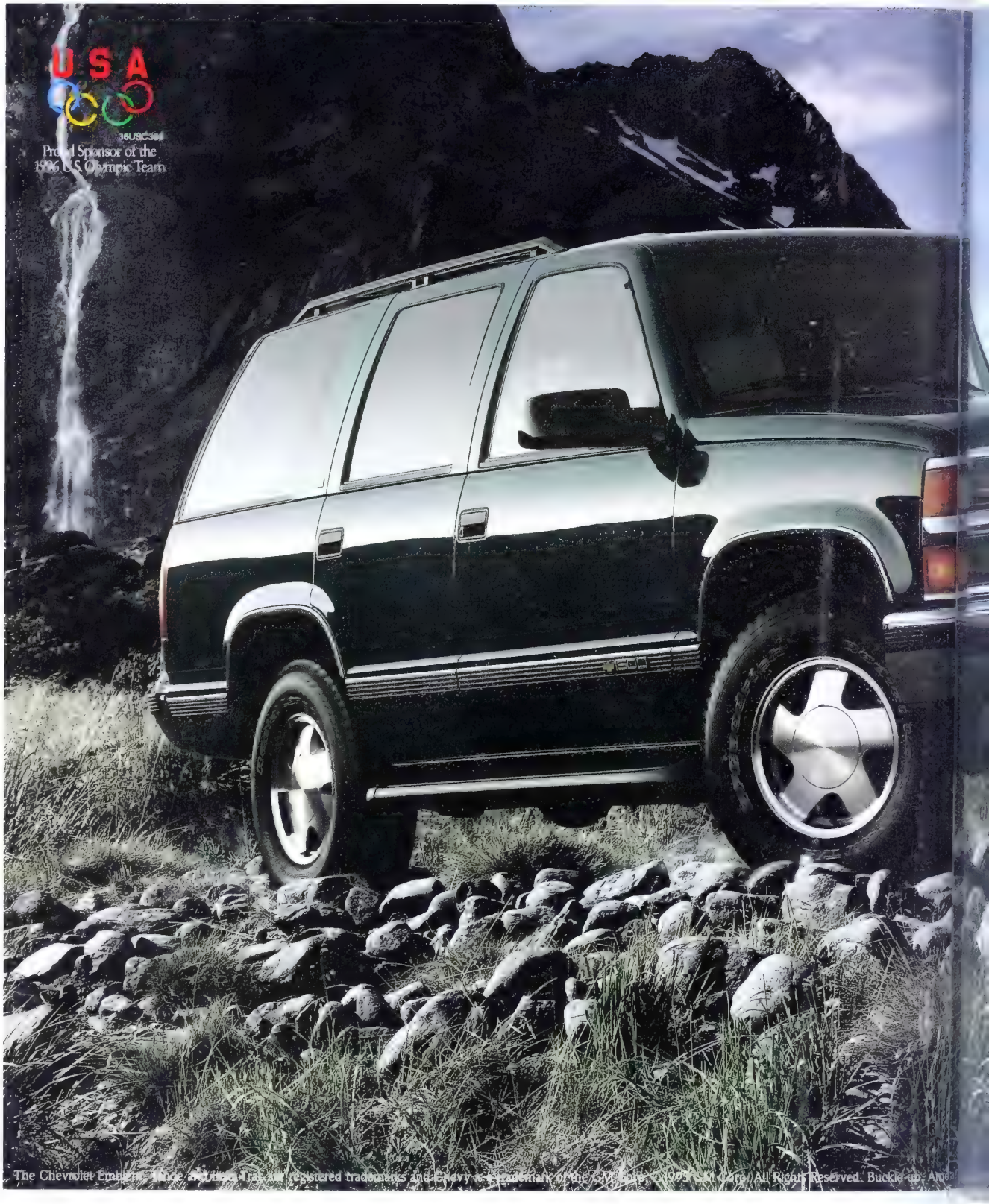

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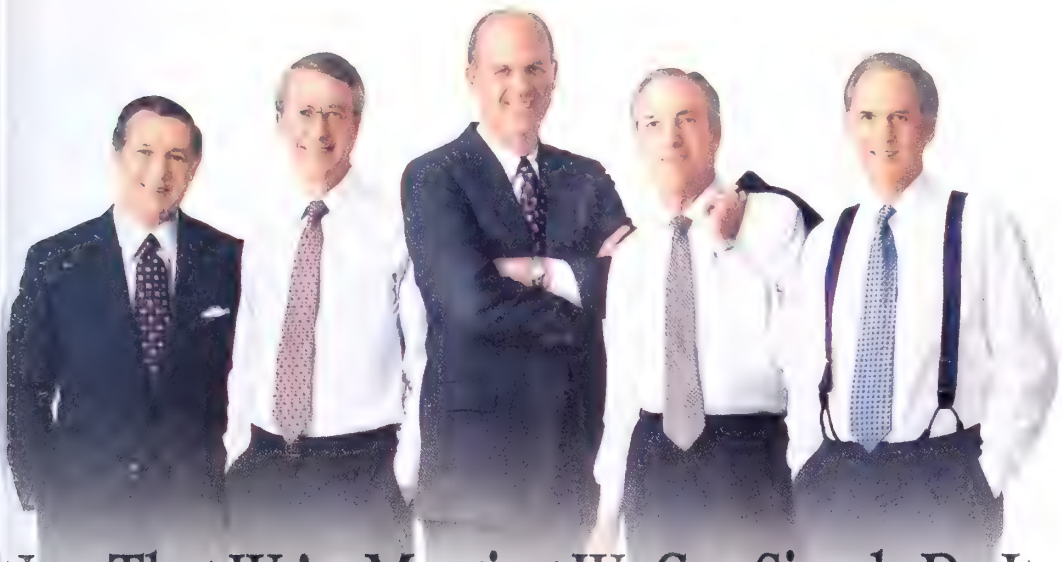
For Years We've Envied Each Other's Capabilities From Afar.

1996 Chemical Banking Corporation and The Chase Manhattan Corporation



Now That We're Merging, We Can Simply Do It From Across The Hall.

Left to right: Ed Miller, President — Chemical Banking Corp., Michel Kruse, Vice Chairman, Global Financial Services — Chase Manhattan Corp
Walter Shipley, Chairman/CEO — Chemical Banking Corp., Tom Labrecque, Chairman/CEO — Chase Manhattan Corp.
Bill Harrison, Vice Chairman, Global Wholesale Banking — Chemical Banking Corp

Chase and Chemical have long envied each other's capabilities. But through it all, there was one trait we both shared: exceptional client focus. That's why our agreed merger is more than just combining our capabilities. It's an integration of our abilities to deliver the best solutions. An integration of people and ideas. It's a leveraging of our leadership positions to identify new opportunities for your business. It's teamwork across all lines of business to solve your individual needs. Whether those needs are on the other side of the street, the other side of the country or the other side of the world.

CHASE CHEMICAL

JAPAN TURNS A CORNER

A rising yen and falling sales gave Japan's Big Four a rough ride. But Detroit had better watch out for them now page 108

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BUSINESS BASHER

Buchanan's primary drive is sending a chill through Corporate America

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Lilly's global reach aids in testing drugs

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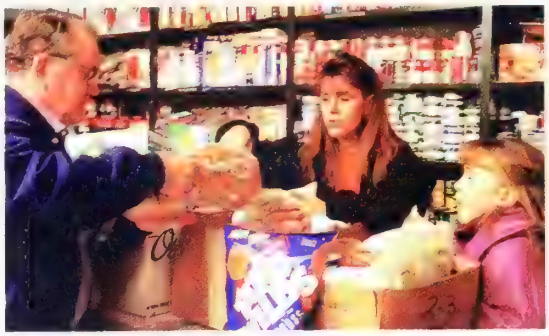

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Small investors are looking savvier than bearish pros page 92

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Nora Slatkin is tackling the CIA's bureaucracy page 114

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CEO Ridder is noted for speed—ne seems to be going nowhere

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What does the GOP really want?
Good fences make for lousy intranets

Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

TALK SHOW "When the voter speaks, I listen—particula if the voter is saying someone else's name."

—Senator Phil Gramm (R-Tex.), bowing out of the Presidential race after his fifth-place finish in the Iowa caucuses

KERKORIAN: *Scouting A.C.*

FAT WALLETS

WILL HE BLOW IT ALL ON THE TABLES?

KIRK KERKORIAN COMES AWAY with a big financial bonus from his truce with Chrysler. So where is the Las Vegas billionaire going to direct his even-heftier financial resources? Atlantic City.

Kerkorian just applied for a New Jersey gaming license. That bodes for a major expansion of his casino operations into booming Atlantic City, where 1995 revenues were up 10%. His agents are busy scouting sites in the area. In Las Vegas, he already owns the MGM Grand, the world's largest hotel, and a half-interest in another huge complex, New York-New York. Kerkorian is also trolling for undervalued companies, much as Chrysler used to do.

Thanks to the pact with Chrysler, he has still more jack to work with. The deal calls for the auto maker to triple its stock-buyback program. Kerkorian intends to use this to cash out some of his 51 million Chrysler shares. Eventually, he could sell the 13.8% stake to Chrysler, or the auto maker may help him find buyers it can live with, says a source close to the Chrysler-Kerkorian talks. "If he does decide to get out, he'll have to work with Chrysler," says the source. *Bill Vlasic*

BANKRUPTCY BLUES

ABOUT THAT BONUS: SEE YOU IN COURT

EMPLOYEES OF MERRY-GO-Round Enterprises, the about-to-close clothing retailer, likely won't receive their promised bonuses, even though the CEO is getting paid in full.

At issue: a so-called "retention bonus" that the chain, which entered Chapter 11 in late 1994, had promised 400 managers and other midlevel employees if they stayed through Jan. 30, 1996. Shortly before Jan. 30, a company memo came out pushing the date to Feb. 3. On Feb. 2, Merry-Go-Round said it would fold and fired everybody. So those promised the retention bonuses, ranging from $750 to $13,000 depending on salary, stand to get zip. Grousing grew even louder when the company, on Feb. 4, rehired 100 to help with the liquidation—sans bonus. Says Buzzy Sklar, men's-merchandise manag "It was a major hosing."

It doesn't help that Richard Crystal, a former exec at Macy's who arri just six months ago, gets pocket $2.5 million so Court filings say that su his salary, was to be spr over three years, but he take it all if he lea before. The liquidat is expected to be d in a few months. company, which wrong on its yo fashions, won't co ment on the pay s ation other than say employees press their claim court. *Roy Furch*

ALL'S NOT LOST: *The boss gets paid*

CAMPAIGN '96

A CORPORATE GADFLY HITS THE STUMP

MONKS: *After a Senate seat*

ROBERT MONKS has had more success as a shareholder activist than as a politician. Yet Monks, for the third time, is seeking a Senate seat from Maine.

Before, he got trounced by venerable incumbents: Republican Margaret Chase Smith (1972) and Democrat Edmund Muskie (1976). But now, Monks, 62, seeks an open seat: Republican Senator William Cohen is retiring. Monks's huge wealth from investing is a big political plus. A longtime donor in Maine politics, he has enlisted top campaign staffers and won key endorsements.

His chief foe in the June 11 GOP primary is Susan Collins, the losing entry in the 1994 governor's race. They'll battle for the moderate vote, creating a possible opening for the arch-conservative third candidate, State Senator John Hathaway. Likely Democratic nominee: ex-Governor Joseph Brennan.

As the gadfly head of the Lens fund, he has pushed for better performance from the likes of Eastman Kodak and Sears Roebuck. He also government experience a top Reagan Administrat pension regulator. Monk pitch is that he can overh Washington as he did cor rate governance. "Pow without accountability," says, "is a problem in g ernment just as it is in c porations." *Mark Maremo*

THE LIST **INVESTMENT 101**

Harvard has the largest endowment, but Emory gets the asset-growth prize for the 1994-95 school year. Main reason: Almost half of its holdings are in Coca-Cola stock, up 53% in the period. Most universities are more cautious—and often trail the market. Harvard's investment return was 16.8%, vs. the S&P 500's 26.1%. It's unclear how much endowment growth is from investment vs. gifts.

EMORY: *Coke is it*

BEST UNIVERSITY ENDOWMENT GROWTH

FOR SCHOOLS WITH AT LEAST $2 BILLION, YEAR ENDING JUNE 30, 1995

UNIVERSITY	ENDOWMENT BILLIONS	GROW RATE
1 EMORY	$2.23	32.0
2 CALIFORNIA*	2.14	22.5
3 WASHINGTON (ST. LOUIS)	2.06	18.5
4 MIT	2.07	16.9
5 HARVARD	7.04	13.6
6 COLUMBIA	2.17	13.3
7 PRINCETON	3.88	12.6
8 STANFORD	3.08	12.3
9 YALE	3.95	12.2
10 TEXAS*	5.04	10.9

*Statewide public university system

DATA: NATIONAL ASSOCIATION OF COLLEGE & UNIVERSITY BUSINESS OFFICERS

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Up Front

PITTSBURGH: *Up from Steeler mugs*

Airmall in Pittsburgh. Opened in 1992, the mall, with a wide selection of popular stores and attractive displays, has tripled per-passenger retail spending to $7 per visit. BAA just signed a 10-year contract to manage all operations, including retailing, at Indianapolis' airport. And the company says it's negotiating with at least eight other U.S. airports. BAA won't name names, but says Los Angeles International and New York's Kennedy have expressed interest in the concept.

Although some people aren't keen on adding carry-on baggage, the Pittsburgh Airmall has done well because passengers are a relatively affluent crowd with little better to do than shop. Also helping sales is BAA's strategy of keeping prices the same as those outside the airport. *Christina Del Valle*

RETAIL TALES

SHOP 'TIL YOU BOARD

THE SHOPPING MAY SOON GET a lot better while you wait for your flight. A British company is pushing to make American airport terminals into small malls, attracting national chains such as Gap. Now, travelers mostly make do with tacky gift shops and newsstands.

The British Airports Authority, a privatized government agency (annual revenue: $1.8 billion), owns and runs seven airports in Britain. It has scored a success with

GENERATION X FILES

WAY COOL MERLOT, MAN

WINE WRITING HAS YIELDED enough daffy and pretentious prose to stop people from ever uncorking a bottle. Now comes a new wine magazine promising straight talk about average-price vintages—and gearing itself to Generation X.

Traditional upscale wine publications, such as *Wine Enthusiast Magazine* (80,000 subscribers) and *Wine Spectator* (115,000), are aimed at connoisseurs and loaded with glossy pictures of sunshine on buxom grapes in Burgundy and celebrities' elaborate cellars. The bimonthly *Wine X* (5,500) is printed in shades of gray on unslick stock, with no photos.

However, the biggest difference is the writing. A recent *Wine Enthusiast* report described a cabernet sauvignon as "dark and chewy with vinous fruit and mint nuances in a sturdy frame." Sounds more like a burned piece of toast. A *Wine X* review says the "nose on this wine is like a neon sign flashing: 'Drink me, drink me.'"

Publisher Darryl Roberts, 33, a former winery worker, says only 4% of Generation Xers drink wine, compared with 35% of the general public. A big reason, he says, is that they're put off by the established mags' mumbo vinbo. *Joan O'C. Hamilton*

DRAWN & QUARTERED

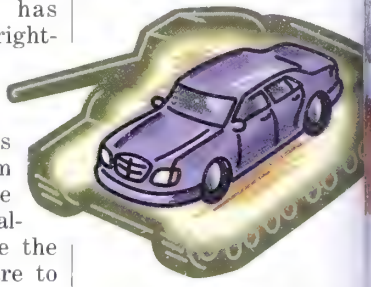
PRODUCT PEEK

MY OTHER CAR IS A SHERMAN TANK

BULLETPROOF CARS AREN'T just for jittery Third World executives or heads of state anymore. A major armor-plated-car company has started to sell kits to frightened Americans.

Overseas, Ogden (Utah)-based International Armoring shields motorists from terrorism and kidnapping. In the U.S., carjacking, vandalism, and break-ins are the problem. Most sales are to people "who've had a bad experience or know a close friend who has," says CEO Mark Burton. One customer bought kits for his car and his wife's after a carjacker threatened him at gunpoint.

The company says the armor can stop a .44 Magn round. And the windows billed as impervious smashing. Plus, Internati al Armoring says the arm is so lightweight—just pounds for four side w dows—that handling and mileage aren't hurt. It h

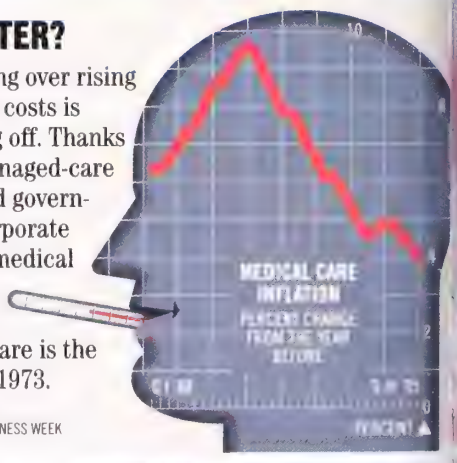


sold 800 kits since their del last spring in the U.S. prices from $2,000 to $12,0 depending on the amount shielding. The kits are stalled by certified technici around the country in two three days. *Sandra Dall*

THE BIG PICTURE

FEEL BETTER?

All the barking over rising medical care costs is finally paying off. Thanks largely to managed-care programs and government and corporate pressure on medical costs, the inflation rate for medical care is the lowest since 1973.



DATA: LABOR DEPT., BUSINESS WEEK

FOOTNOTES Share of employers offering flextime: 73%; who allow working at home: 19%

NOW, THE INTERNATIONAL POWERHOUSE IN FOODSERVICE HAS AS MUCH TO DO WITH GLOBAL ECONOMICS AS IT DOES WITH FRESH INGREDIENTS.

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oks up with mate on a seasonal basis

has convenient off-line capabilities

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compatible with most hardware and software

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there's nothing like it

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Readers Report

ON APPLE'S BRUISING

Regarding your article "The fall of an American icon" (Cover Story, Feb. 5), the Macintosh is the closest thing to an appliance that the computer industry has ever created. But that doesn't excuse Apple's years of arrogant disregard for market realities: Stubborn refusal to license its operating system (history demonstrates the folly in trying to use proprietary technology to capture a market); misguided advertising (Apple "preaches to the choir" by placing its most creative, informative ads in Macintosh-oriented trade publications); and an inability to take advantage of windows of opportunities. Apple has a track record for leading-edge technology. But its technical prowess is overshadowed by its business knack for repeatedly snatching defeat from the jaws of victory.

Martin H. Tesler
Alexandria, Va.

WHAT FALL?

"May I point out that Apple has experienced only one bad quarter and actually was profitable for the fiscal year."

Your cover caption ranks with the O. J. trial for incredibly irresponsible reporting. May I point out that Apple has experienced only one bad quarter and actually was profitable for the fiscal year. And that many other major companies such as AT&T, AST, Daimler Benz, and Xerox have reported losses that are 10, 20, 30 times larger without their immediate demise being proclaimed.

And may I point out that it is Apple's leading technology and superior engineering that leads the desktop computer revolution. Everything that Microsoft produces today was first developed by Apple engineers. Sadly, Microsoft then releases Apple's ideas in an inferior form and gets rave reviews for them. And further, Macintosh users are far more loyal than those of practically any other company. The reason is simple: We know we reap the benefits of the most advanced, easy-to-use technology that exists in the market today. Customer satisfaction su
veys prove it.

John Colli
Newport Beach, Ca

You paint a picture of a compa
bent on self-destruction: an indust
leader led down the garden path by
anarchic throng of selfish managers. Y
Apple's stock price was still 1.5 tim
book value when your article appear
whereas when IBM and Digital Equ
ment were in their troubles, they we
at about 0.5. Does this say somethi
about what the market thinks? Desp
all Apple's crises, the company still h

key strengths in multimedia, deskt
publishing, education, Internet serve
and, yes, with software developers.

Benjamin Ostro
Madison, N.

As a platform buyer of Apple co
puters, I am telling you that no amou
of media propaganda is swaying a
buying decision I make. Macintosh
work gracefully on all tasks includi
data management. They integrate
fectively and reliably on the netwo
and have outstanding performance a
RISC platform scalability. With the c
rent platform of PCI-based Power Ma
intosh computers, I have never be
more confident in our platform decisio

Gary Heinon
Director of Syste
Mars Advertisi
Southfield, Mic

How can you, with clear conscien
tout Apple as a fallen company, whi

Business Week
A Division of The McGraw-Hill Companies

FEBRUARY 26, 1996 (ISSN 0007-7135)*** 3464
Published weekly, except for one issue in January, by The McGraw-Hill Companies, Inc. Founder: James H. McGraw (1860-1948)
Executive Editorial, Circulation and Advertising Offices: The McGraw-Hill Companies Building, 1221 Avenue of the Americas, New York, N.Y. 10020. Telephone (212) 512-2000. Telex: Domestic 12-7960, International 62-7960. Cable address: McGRAW-HILL NEWYORK. Subscription prices: $79.95 a year; $99.95 outside U.S. Single copies, $2.95, back issues, $5. Write for rates in other countries. Subscriber Services: 1-800-635-1200. TDD: 1-800-554-1579

Postmaster: Send address changes to BUSINESS WEEK, P.O. Box 430, Hightstown, N.J. 08520. Periodicals postage paid at New York, N.Y. and additional mailing offices. Postage paid at Montreal, P.Q. Canada Post International Publications Mail Product Sales Agreement No. 246484

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using their product to lay out your own magazine? Do your writers speak to your art directors? Apple Computer has something that none of its competitors have. In fact, I can only think of a handful of companies globally that share it. They have a following! Mark my words: Your readers will stop reading BUSINESS WEEK long before we stop buying Macintoshes!

Foster Bass
Cambridge, Mass.

How about a story of how the media has been consistently predicting the demise of Apple Computer since its inception, and how they have been consistently wrong?

Ian D. Brazier
Graduate School of Management
University of Queensland
Australia

BUSINESS WEEK readers deserve clarification regarding last week's Cover Story about Apple Computer and its advertising. I was managing the Apple account when the now-famous "1984" television commercial was produced. The notion that the "1984" commercial "was shown only once" is a myth. It actually ran a week prior to the Super Bowl in 13 spot markets. One of these, by design, was Boca Raton, where the IBM PC division was situated.

Fred Goldberg
Chairman/CEO
Goldberg Moser O'Neill
San Francisco

IS USAIR GETTING A SAVIOR IN STEPHEN WOLF?

Your snide comments regarding Stephen Wolf in "Back in the cockpit" (In Business This Week, Jan. 29) were really out of order. While Mr. Wolf may make a significant personal gain as the new CEO at USAir Inc., the point of your story should have been the potential for gain to the owners of USAir that he brings to the table, just as he served the owners so well at Republic, Flying Tiger, and especially United Airlines. To suggest that Wolf has a "bad guy" image or that he "beat up on employees" is wrong. He brings to the airline business the skills of emphasizing what is right about an airline—so that more customers use it—and the stockholders benefit. If that means some people with attitudes inappropriate for a customer-service business suffer, so be it.

Roger J. Baccigaluppi
Chairman
RB International
Sacramento

CORRECTIONS & CLARIFICATIONS

"Not all tax software is created equal" (Personal Business, Feb. 5) listed the incorrect developer of Kiplinger TaxCut. TaxCut is produced by Block Financial Corp.

"Butterfly on a pin" (Up Front, Feb. 19) erroneous listed the weight of IBM's Kite notebook PC. It will be 4.5 pounds. The item also incorrectly listed the new price for the Butterfly: It's now priced from $1,499 to $2,299.

I am tired of hearing about Stephen Wolf, the savior of United Airlines Inc. He agreed to excessive labor contracts that led to financial difficulties (this is the part that is usually not mentioned), and then he gave up half of the company to buy United out of the agreements. Where is the genius in that? The shareholders lost half of their company to pay for the mistakes of Wolf and his management team. But of course, there is real genius involved—Wolf walks away with millions of dollars for his fine work.

I hope the shareholders of USAir make out better.

Paul R. Knapp
Chicago

MAKING SENSE OF WASHINGTON STAGNATION

In response to your article "The Politics of Stagnation" (Editorials, Feb. 5), since FDR's first term, government has taken control of more and more of our lives so that now, any government action or policy virtually affects all of our lives. With such high stakes, it is imperative that each of us fight a battle for what we want on every issue. I am delighted to see stagnation in Washington over the issue of whether the government should spend a little more or a lot more on health, education, welfare, policing the world, foreign aid, disaster relief, subsidizing real estate, subsidizing the arts, immigration, and God knows what else it does.

Jim Johnson
Lomita, Calif.

CATHAY'S CONFIDENCE IN THE BOEING 777

I refer to "Did the FAA go easy on Boeing?" (The Corporation, Jan. 29). The story claims that in 1993, a Cathay Pacific Airways Ltd. Boeing 747 aircraft flying out of Los Angeles suffered "such severe vibrations that the pilots considered ditching the plane in the sea." Th is pure fantasy. The fan-blade failur on the flight is the only case in 60 mi lion hours of operation of the RB21 family of engines, and the fact is, ai craft are designed and built to with stand such events. The aircraft co cerned was fully controllable at a times, and ditching the aircraft neve crossed the captain's mind. In fact, h eased the vibration by slowing dow the aircraft and then returned to Lo Angeles. The aircraft made its flight 1 hours later after an engine change an has never experienced any in-servic problems since. You may be intereste to hear that the captain of the 199 Cathay Pacific flight referred to in th article has expressed a keen interest flying the 777, which we and many oth er airlines have ordered.

C.F. Kwa
Manage
Corporate Communicatio
Cathay Pacific Airway
Hong Kon

Editor's note: BUSINESS WEEK's comments on the 747 fan blade failure which raised concerns within the Federal Aviation Administration about the much larger 777 engine then under development, were based on an FAA briefing paper. The Feb. 24, 1995, paper said as a result of the failure, "severe vibration levels were experienced as the engine windmilled. The flight crew declared an emergency and was considering ditching the airplane because of concern for structural integrity." Two FAA sources independently confirmed the incident's severity.

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THE LAST STAND
The War Between Wall Street and Main Street Over California's Ancient Redwoods
By David Harris
Times • 373pp • $25.00

A 1980s CHAINSAW MASSACRE

To walk through the few surviving stands of Northern California coast redwoods is like taking a journey into the primordial past. For aeons before humans came onto the scene, the trees existed in mist-shrouded obscurity, serving as home to an extraordinary array of wildlife. But all of this is secondary to Texas financier Charles Hurwitz, to whom the ancient forests' only value is economic. A single old-growth tree equals about $30,000 worth of lumber.

Even by the rapacious standards of the 1980s, Hurwitz' 1985 hostile takeover of Pacific Lumber Co. stands out, largely because it precipitated an assault on the 183,000 acres of redwoods acquired in the deal. But according to the Darwinian rules of 1980s' dealmaking, Hurwitz had little choice. Financed with more than $800 million in junk bonds, the Pacific Lumber deal only worked if Hurwitz serviced the debt by doubling, then tripling, the rate of lumbering. And if he could clear all of the old-growth trees, Hurwitz figured that he would end up $1 billion ahead.

In the frenzy to cut trees, Hurwitz also managed to overturn a well-run family business and to bring chaos to Scotia, Calif., the small company town where Pacific Lumber's mills had provided steady jobs and strong community bonds for more than five decades. And he aroused the rage of a small band of militant environmentalists who fought the financier every step of the way.

This sad story is told in all its gritty detail in *The Last Stand*, David Harris' riveting book, in which almost no one comes out looking good. Harris, a former contributing editor to *The New York Times Magazine* and *Rolling Stone*, has produced a work that reads more like a Raymond Chandler novel than a piece of journalism. Moving seamlessly from the action on the high-yield trading desks in New York and Beverly Hills to small-town gossip sessions at the local Scotia diner to meetings of the disheveled Earth First! protesters, Harris weaves a tapestry of mounting intrigue and impending danger.

Along the way, the author provides a nostalgia trip through the wild days of junk-bond dealmaking. Assisting Hurwitz is a Who's Who of 1980s operators. Drexel Burnham Lambert, Hurwitz' investment banker, conducts a surreptitious aerial survey of Pacific Lumber's timber holdings. Then, Harris writes, Drexel's Michael Milken, with a wave of the hand, agrees to peddle the junk bonds to his network of customers, while Ivan Boesky and Boyd Jefferies quietly park big chunks of Pacific Lumber shares until Hurwitz is ready to pounce. Later, it is Milken's buddy, Fred Carr, who helps Hurwitz tap the "overfunded" employee pension fund through his insurance company, First Executive Corp.

Harris excels in describing the transformation of Pacific Lumber and the town of Scotia following the takeover. For decades, the company's founders ran it like a big extended family. Despite legendary boom-and-bust cycles in the lumber industry, the townsfolk in Scotia enjoyed steady work. The reason: Since the 1930s, Pacific Lumber fiercely adhered to a conservative harvesting program, each year selectively cutting just the amount of board feet that it figured would grow back.

And Pacific Lumber supplied more than steady jobs. Unlike at other mills, Harris says, workers enjoyed pensions, health benefits, and an employee [illegible] plan, while every kid who won a [illegible] sion to college got a scholarship. Pro[illegible] vided cradle-to-grave corporate wel[illegible]

Into this Frank Capraesque [illegible] burst Charles Hurwitz. At first, H[illegible] witz brought a nice windfall. Ro[illegible] the-clock operations produced extra[illegible] for new pickup trucks and washing[illegible] chines. But soon, the town seem[illegible] lose its bearings, injuries mount[illegible] the mill, and, when Hurwitz siph[illegible] cash from the pension fund, wor[illegible] mounted their own buyout plan, w[illegible] eventually proved unsuccessful.

Ultimately, though, it was the [illegible] frontation between Pacific Lumber[illegible] Earth First that laid waste both to [illegible] witz' plans and Scotia's well-b[illegible] Clear-cutting of entire old-gr[illegible] stands—"monster trees that yielde[illegible] best softwood in existence"—spark[illegible] series of tumultuous protest ma[illegible] and a string of lawsuits that ha[illegible] this day suspended logging in th[illegible] cient grove known [illegible] Headwaters Forest. [illegible] witz, it seems, [illegible] underestimated the p[illegible] of the environmenta[illegible] With production down [illegible] offs have soared. But [illegible] of clear-cutting destr[illegible] irreplaceable forests.

As compelling as [illegible] *Last Stand* is, the [illegible] could use some cuttin[illegible] its own. As the a[illegible] shifts from the boardr[illegible] to the backwoods of [illegible] berville, the enclave w[illegible] the Earth First organizers hold [illegible] meetings, the pace slows to a cr[illegible] And while most of the writin[illegible] straightforward, at times Harris [illegible] too hard. "Night had fallen like a [illegible] iron safe down an elevator shaft," [illegible] writes.

But these are minor faults. *The* [illegible] *Stand* is provocative, and it's good [illegible] tertainment. In an age when "maxi[illegible] ing shareholder value" has becom[illegible] corporate mantra, Harris' account [illegible] lenges us to hold corporations to a h[illegible] er standard. Shareholders count f[illegible] lot. But so should workers and [illegible] environment.

BY ERIC SCH[illegible]

Schine covers forest industries [illegible] the environment from Los Angeles

HOW DREXEL DEALMAKERS AND MILITANT TREE-HUGGERS DESTROYED A LUMBER TOWN

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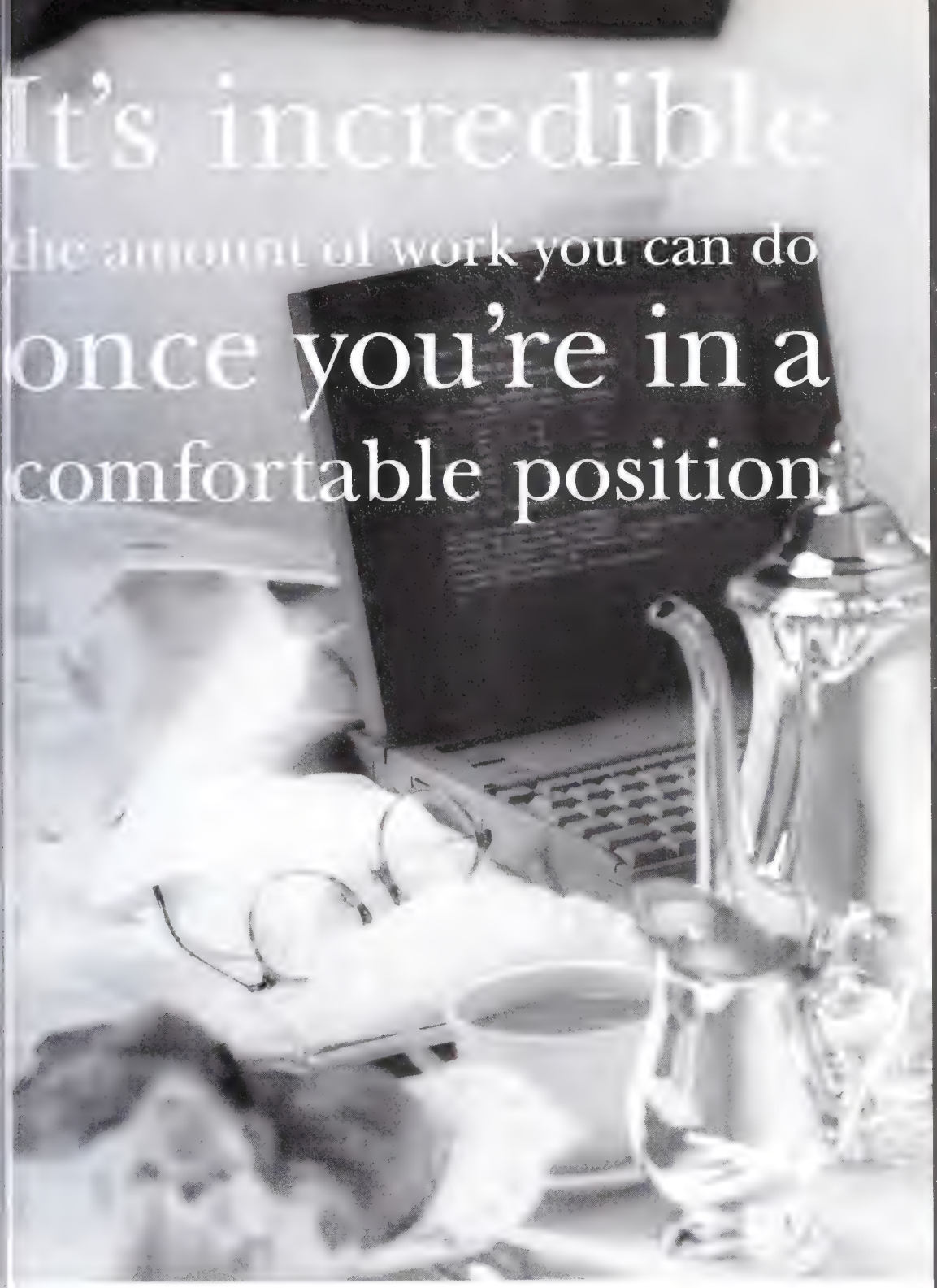

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INESS WEEK's Best-Seller List is based on a survey of chain and independent booksellers that carry a broad selection of books on economics, management, sales and marketing, small business, investing, personal finance, and careers. Well over 1,000 retail outlets nationwide are represent- Current rankings are based on a weighted analysis of unit sales in January.

HOT TYPE

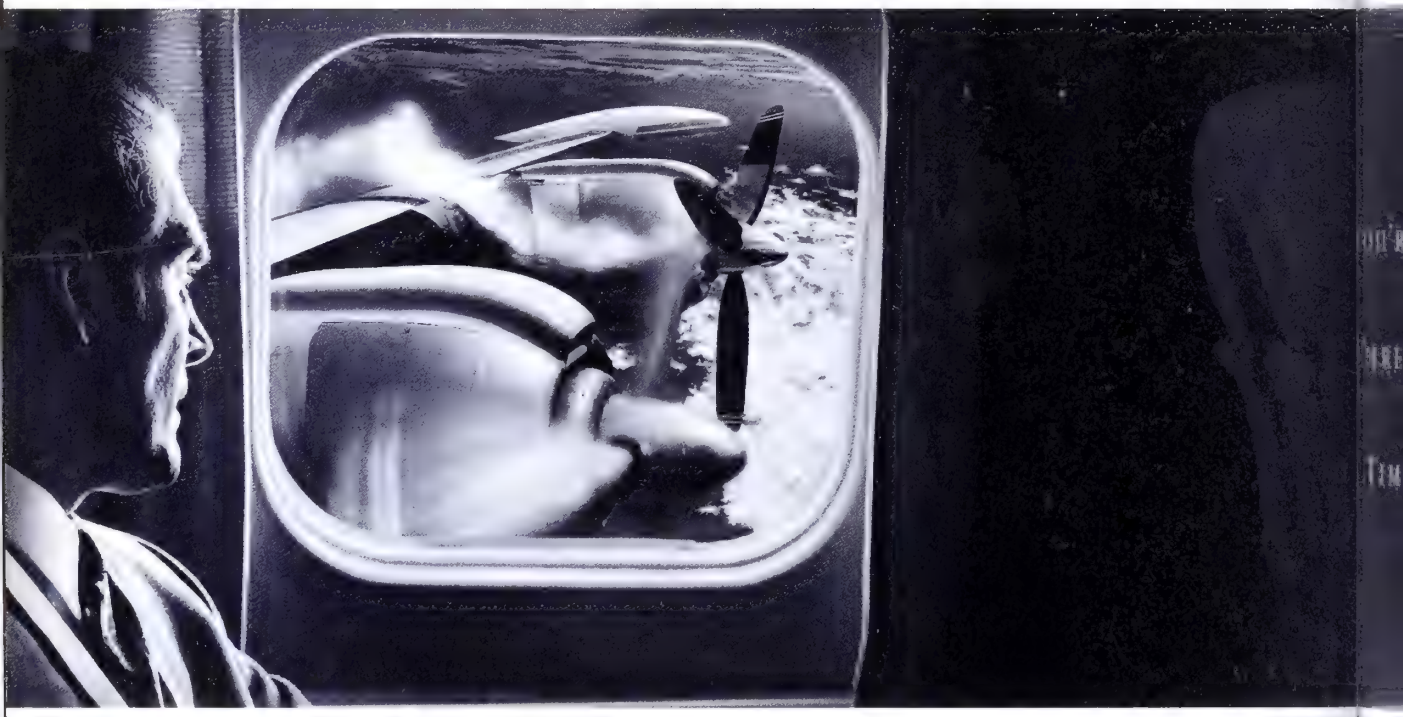
Peter Lynch has a beef with American education: It doesn't teach the basics ıvesting. As a result, says the former manager of Fidelity stment's Magellan fund, many Americans don't start in- ng until late in life, forgoing years of profitable returns. In third book, *Learn to Earn: A Beginner's Guide to the Ba- of Investing and Business* (Fireside), written with John ıchild, Lynch tries to fill the void in investment education a capsule history of capitalism. This month, *Learn to* is No. 3 on BUSINESS WEEK's paperback Best-Seller List. ew are better qualified to explain investing than Lynch, best money manager of the 1980s. But those looking for ı insights will find little beyond what Lynch has already written in two prior books, *Beating the Street* and *One Up on Wall Street*. The Gospel According to Lynch remains the same: Buy stocks and hold them.

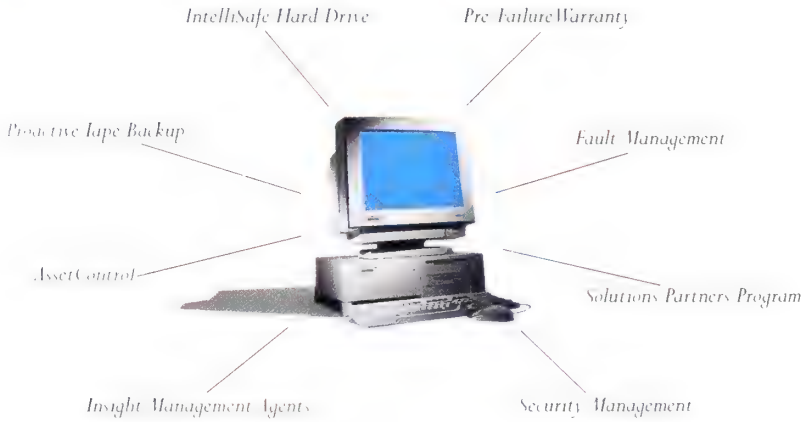
There are some new details in *Learn to Earn*, including an explanation of how to read stock tables and a discussion of price-earnings ratios. But most of the book is a defense of capitalism. Lynch wants to persuade people to trust corporate leaders. "There's a mistaken idea floating around that people who do things for profit are being greedy or underhanded . . . because whenever one person makes a bundle it's at the expense of everybody else," Lynch writes. Instead, he argues, smart investors embrace those who create society's wealth.

BY GEOFFREY SMITH

COMPAQ

Has It Changed Your Life Yet?





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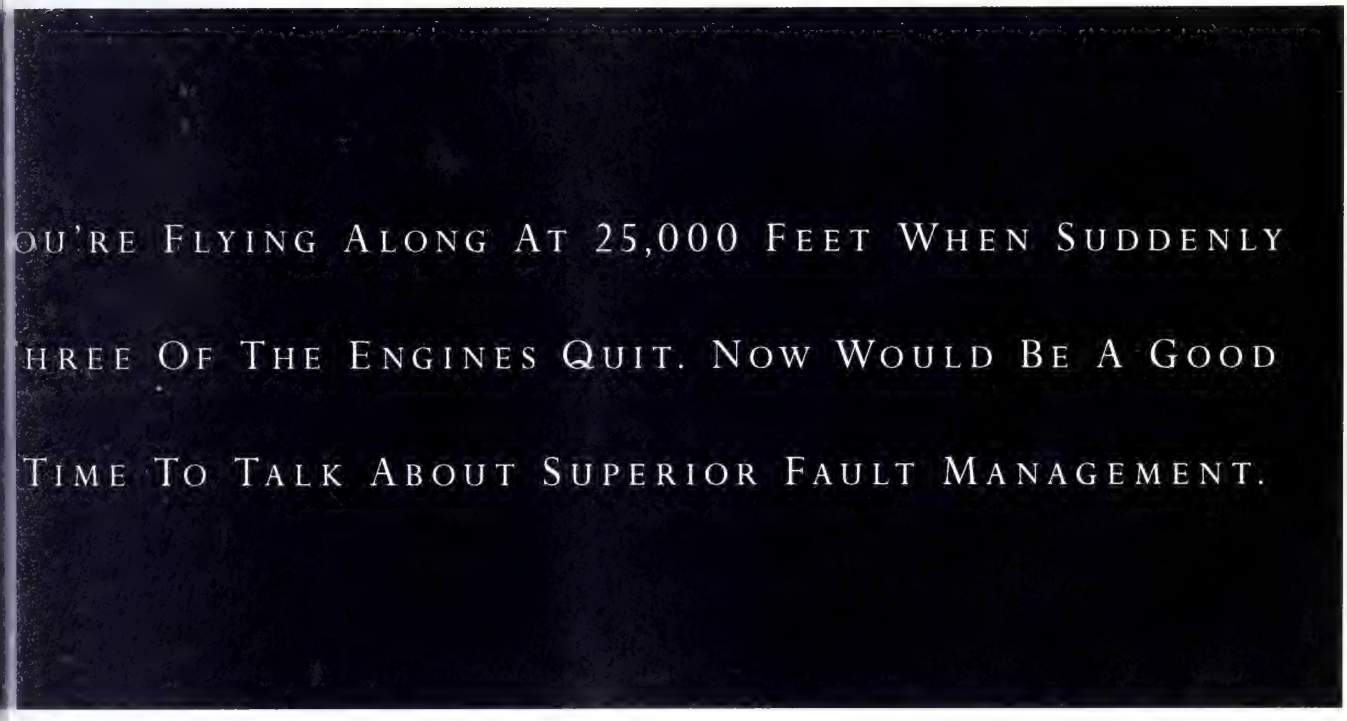

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BY STEPHEN H. WILDSTROM

NO-FRILLS LAPTOPS

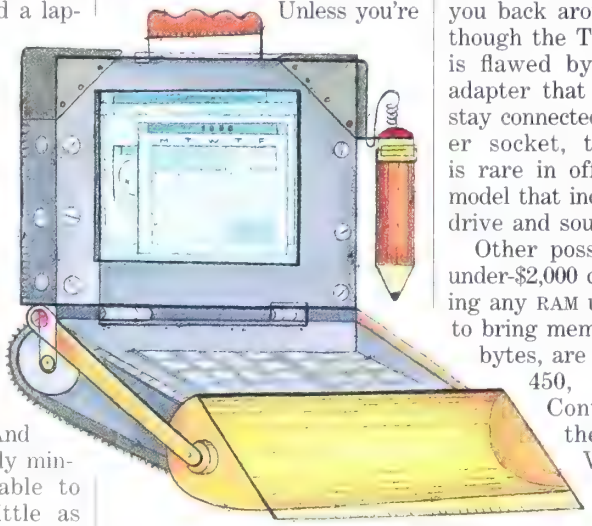
There are many serviceable portables that can be had for less than $2,000

Laptops today come with everything: CD-ROMs, fast Pentium chips, lots of memory, big hard drives, big screens, and big price tags. These high-end machines are a blessing if you do multimedia presentations or heavy-duty financial analysis on the road. But what if you just need a laptop to keep in touch with your E-mail, knock off a memo or two, or do a little light spreadsheet work while you're traveling?

There's no reason to spend $6,000, or even $3,000, for a light-duty laptop. For less than $2,000, you can get a serviceable machine; for $2,500, a somewhat luxurious one. And if your needs are truly minimal, you may be able to scrape by for as little as $1,000. A 14.4 kilobits-per-second PC Card modem will add about $150, a 28.8 kbps modem about $250.

SLOW PROCESSORS. In laptops, like everything else, you still get what you pay for, and portables in this price range aren't the latest and greatest. Pentiums are just starting to appear in computer makers' "value line" notebooks. Most use 486 processors and, at the very low end, slow ones. Screens will be passive matrix, which are not as bright as active matrix. The disk drive may be only 340 megabytes. The battery will be nickel metal hydride, not longer-lasting lithium ion. And, of course, there will be no CD-ROM drive or sound. You can get a machine from top-line vendors, including IBM, Compaq, Toshiba, and Texas Instruments, though it may be a unit that has just been, or soon will be, discontinued.

What's the minimum you should look for in a laptop? Unless you're sure you will never run Windows, I'd avoid the few stray monochrome machines out there, as well as anything with less than 8 megabytes of memory. I wouldn't consider a processor slower than a 50 megahertz 486DX nor a hard drive smaller than 340 megabytes. Unless you can get by with the barest minimum, avoid, for example, the Compaq Aero 4/33. Although its widely advertised price of $1,000 and its light weight make it attractive, it is simply too underpowered to meet most users' needs.



I would also go for a laptop with Windows 95 installed. If it isn't already loaded, make sure that Win95 will work with that machine. Whatever the debates over the merits of Win95 on desktops, its superior communications support, handling of PC Card accessories, and power-management capabilities make it the clear choice for laptops. But some notebooks made before last July may have problems running Win95.

FLAWED DESIGN. This still leaves you with an abundance of choices below $2,000. For example, you can find the Toshiba T2110CS for around $1,650, though you should expect to spend another $250 or so for an extra 4 megabytes of RAM. A basic IBM ThinkPad 365CS will set you back around $1,800. Although the ThinkPad design is flawed by an AC power adapter that doesn't like to stay connected to its computer socket, the 365 series is rare in offering a $2,500 model that includes a CD-ROM drive and sound.

Other possibilities in the under-$2,000 category, including any RAM upgrade needed to bring memory to 8 megabytes, are the TI Extensa 450, the Compaq Contura 410c, and the NEC Versa V/50C. Perhaps the greatest bargain out there is the orphaned AT&T Globalyst 130. Rumerson Technologies (800 929-0029), liquidator of AT&T's computer inventories, is selling the Globalyst for $1,450.

By the end of the year, these 486-based machines are likely to disappear from product lists and inventories, to be replaced at the low end by 75-megahertz Pentiums. But if you don't need a state-of-the-art portable, any of these computers will likely meet your needs for at least the next couple of years.

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SOFTWARE

POLYGLOT PROGRAMS

Business is getting more global every day, but few computers do more than one language well. Those who need strong multilingual features can get help from a line of Windows programs from Accent Software International (800 535-5256).

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BY ROBERT KUTTNER

REWARDING CORPORATIONS THAT REALLY INVEST IN AMERICA

BLUEPRINT: Workers and communities have a stake in companies, too, and a proposal in Congress would recognize that

Two leading Senate Democrats will soon release an election-year proposal that could reopen the debate about the corporation's social purpose. Minority Leader Thomas A. Daschle (D-S. D.) and Jeff Bingaman (D-N. M.), who heads Daschle's task force on living standards, propose a new kind of federally chartered corporation. It comes at a time when productivity gains go mainly to shareholders rather than employees and no one appears to know how to raise wages and salaries.

Bingaman and Daschle have therefore turned to the one avenue that might produce some traction: inducing corporations to embrace a "stakeholder" model. The draft legislation, to be released in late February, proposes a new class of corporations, the R Corp.—"R" for Responsible. The idea is to reward corporations that invest in employees and communities instead of pursuing relentless downsizing that boosts short-term profits.

An R Corp. would receive lower taxes and streamlined regulatory treatment. Specifically, the plan replaces the corporate income tax with a "business activity tax" of the sort proposed in 1994 by Senators John C. Danforth (R-Mo.) and David L. Boren (D-Okla.). This tax applies a fixed rate to all receipts, subtracting payments for most inputs. Employee training and R&D expenses would be tax-deductible, while wages, dividends, and interest would not. Under this plan, an R Corp. would be taxed at 11%, compared with 18% for conventional corporations. It would also pay reduced payroll taxes and be able to self-certify in several areas of regulation.

COMPENSATION RATIO. To qualify, a corporation would have to meet several tests. It would be required to contribute 3% of payroll to a portable, multi-employer pension plan, devote 2% to employee training, pay half the costs of a qualifying health plan, and have a profit-sharing plan or employee stock ownership plan with employee trustees.

Another requirement would be to hold the compensation ratio of the highest- to lowest-paid employee to no more than 50 to 1, compared with the 130-to-1 ratio in some corporations. An R Corp. would have a "community responsibility agreement" tempering relocations and layoffs. It would be unionized or have an employee-involvement plan. An R Corp. could not use child or prison labor anywhere in the world and half of its new investment and employment would have to be the U. S.

The Bingaman plan includes a tax of t sort long proposed by Yale University econ mist James Tobin on the profits of short-te securities trades. The proceeds would finance social capital fund for worker training, scho to-work transition programs, industrial exte sion, export promotion, and technology r search and development.

HOWLS OF INDIGNATION. This unabashedly terventionist plan will likely bring howls of dignation from champions of unfettered ma kets. But it frames an overdue debate corporate accountability and the cure f short-termism. Throughout the 1980s, t choice was between avenging corpora raiders or stagnant, entrenched manage Some choice. The corporation was seen accountable solely to its shareholders, not t broader community of stakeholders. T shareholder-rights movement, spearhead by large pension funds, supposedly offer an alternative of more patient capital. B often these supposed long-term owners pu sued short-term returns.

The Bingaman plan suggests that we need choose between the imperfect discipline of tra ing markets and the imperfect inertia of t manager-dominated corporation. The stak holder approach invokes an older, more soc conception of the joint-stock company—whe not only the shareholders but also employe and communities have a legitimate stake the enterprise.

Liberals, left out of the raider-vs.-manag debate about corporate governance, seem to converging on this idea. Senator Edward Kennedy (D-Mass.) has proposed a very simil strategy. And the idea of "stakeholder ca talism" is becoming the signature proposal the new British Labor Party leader, Tony Bla U. S. Labor Secretary Robert B. Reich r cently wrote in a *New York Times* Op-Ed pie that "the corporation is, after all, a creation law. If we want corporations to take more r sponsibility, we will have to alter [their] mix advantages and disadvantages to provide t proper incentives."

The Bingaman blueprint does just that. remains to be seen whether Reich's boss w embrace it, but after years of being on t defensive, Democrats are coming to life by f cusing on the issue of how to raise living sta dards and the purpose of the corporation.

Robert Kuttner is co-editor of *The American Prospect* and author of *The End of Laissez-Faire*

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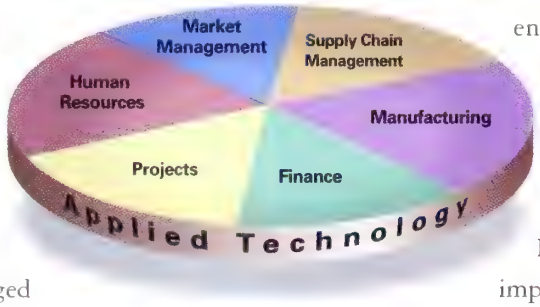

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BY GENE KORETZ

IS THE ECONOMY THAT WEAK?

First factor in the demographics

Recent sluggish business reports, combined with broad-based downward revisions of economic data, are fueling recessionary fears. But economists Roger E. Brinner and David S. Wyss of DRI/McGraw-Hill point out that such reports need to be interpreted in the context of a development that has received too little attention: a mild demographic slump that is affecting the U. S. and most other industrial nations.

In the 1970s, America's adult population expanded at close to a 2% annual rate and the labor force exploded at a 3% pace. By the first half of this decade, however, the 18-to-65-year-old contingent was growing at a scant 0.7% rate. And with labor-force participation by women finally leveling off, growth of the labor force had fallen to a 1.1% annual rate—a pace it is expected to maintain into the next century (chart).

Since economic growth over the long haul is determined by labor input plus productivity gains, the slowdown in growth of the labor force has inevitably lowered the speed at which the economy can expand. This is doubly true because government data revisions indicate that productivity growth in the expansion has averaged just 1.1% to 1.2% a year, far slower than in earlier expansions.

Even if productivity growth speeds up a bit, Brinner and Wyss contend that weak economic data need to be viewed more positively in light of the current demographic slump. Monthly gains of 100,000 jobs, they write, should be welcomed, not mourned. Such data "project not a temporary lull but sustainable growth for a long period."

TROUBLE FOR CARS, HOUSING

But boomers may save the day

The two key industries whose fortunes are most likely to be adversely affected by slowing population growth over the next five years are housing and autos. That's because these businesses especially cater to adults aged 25 to 44—exactly the groups whose growth has slowed sharply in the 1990s.

DRI/McGraw-Hill notes that the number of households headed by 25- to 34-year-olds, which climbed at a heady 4.6% annual clip in the 1970s and rose at a 1% rate in the 1980s, has been contracting in recent years and will decline even more rapidly from 1995 to 2000. And the growth of households headed by 35- to 44-year-olds will slow to an average annual rate of 0.7%, compared with 2.2% in the first half of the 1990s and 3.9% in the 1980s.

For vehicle manufacturers and homebuilders, all of this spells sluggish sales growth through the turn of the century. Single-family home construction, says DRI, will flatten. With modest growth in the number of total drivers, demand for new vehicles is likely to rise slowly by historical standards.

The saving grace in the outlook is the explosive growth of aging baby boomers, who spend more lavishly on cars, appliances, and homes than do younger families. The relatively affluent 45- to 54-year-old cohort of households will expand at a 3.6% clip over the next five years. Thus, to ride out the demographic storm ahead, DRI warns, manufacturers and builders will have to adapt their products to the needs of this well-heeled group that will be upgrading the quality of its purchases.

MORE TEENS ARE LIGHTING UP

A decade-long decline has ended

To a large extent, the success of the battle to reduce smoking in the U. S.—and the health costs it entails—rests on discouraging the habit among teenagers. And by that criterion, the latest results of an annual nationwide survey by the University of Michigan's Survey Research Center indicate that the battle is being lost.

Last year, some 34% of high school seniors reported they had smoked cigarettes during the previous month. That up from 28% in 1992 and 29% to 30 over the prior decade—a range the fi ure had fallen to after approaching 40 in the mid 1970s. Researchers note th 1995 marks the third straight year which the percentage of high scho smokers has registered an increase.

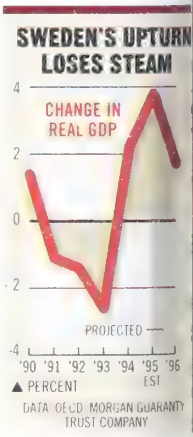
DOWNSIZING THE WELFARE STATE

Is Sweden's resolve wavering?

Swedish policymakers seem to b turning back the clock, reports eco omist Michael Dicks of Morgan Gua anty Trust Co. In the early 1990s, Sw den suffered its worst economic cris since the 1930s, as the economy co tracted for three straight years, unem ployment soared, and the krona was d valued sharply, by 20% in real terms.

In the wake of the crisis, the go ernment acted to put its fiscal house i order by cutting spending, privatizin government enterprises, slashing th top marginal tax rates, and lowerin jobless benefits. Aided by currency d valuation, exports have boomed, an Sweden's economic growth last year wa among the highest in Europe. The go ernment announced plans to balance th budget by 1998, and the Riksbank se an inflation goal of just 2%.

Unemployment, however, has staye high, and the ruling Social Democrat Labor Party's popularity has waned. A a result, Finance Minister Göran Persson, who is expected to become prime minister in March, recently announced plans to raise jobless benefits in future years and loosen other constraints on government spending. And amid signs that Sweden's economy is slowing in line with European sluggishness, the Riksban has been lowering interest rates.



The upshot is growing market fear that cuts in welfare state spending wi be reversed, undermining the credibilit of Sweden's budgetary and inflatio goals. As elsewhere in Europe, risin public concern over unemployment i affecting economic policy.

AMES C. COOPER & KATHLEEN MADIGAN

HY RISING PAY N'T COURTING INFLATION

U.S. ECONOMY Is inflation creeping back into the picture? Several recent lopments make you wonder: surging gold prices, er commodity prices, anecdotal evidence of short- of skilled labor, and last year's increase in core in- n, which excludes energy and food. True, the rise small, but it was the first in five years.

r the surest tips on price pressures, look to the market, since labor makes up some 70% of the of producing U.S. output. Although the latest are a bit old (delayed by the prolonged govern- shutdown), the trends in wages and benefits, uctivity, and unit labor costs support the view consumer prices will grow by 3% or less in 1996 he fifth year in a row.

PRICE PRESSURES WAGES OR BENEFITS

At the same time, increased labor demand, especially for skilled workers, and past productivity gains mean that, after a decade of stagnation, real wages are growing. The gain in buying power will lift consumer spending, if at a modest pace. The bad news for consumers is that slower economic growth means that companies eager to maintain profit surge of recent years will continue the ng downsizings" that have become a fixture in this omy. And lower-skilled workers will still struggle.

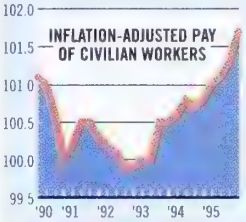
LABOR DEPT.'S employment cost index is signal- hat all is quiet in inflation's corner (chart). The h-quarter ECI for all compensation rose 0.9% from third quarter, and for the year it was up only , a record low. That growth rate was slightly be- 1994's 3% increase, and it marked the sixth consec- year of downtrend.

st quarter's advance was pushed up by a 1.3% in benefits costs. That increase reflected pay- of bonuses, which are becoming a more wide- d form of compensation, and a reversal of the re- downtrend in the pace of health-care costs. Still, h-care inflation is the lowest in more than two les, and overall benefits were up only 2.8% for the also a record low. Straight pay in the form of s and salaries rose only 0.7% last quarter, the as in the two previous quarters, and it was up for the year.

course, some occupations are garnering bigger raises than others. White-collar employees, particularly those in executive and managerial positions, did better than blue-collar employees last year. Although the Labor Dept. does not break out cost indexes for specific jobs, this split offers some evidence that higher-educated, better-skilled workers are in hot enough demand to command higher wages.

This cost pressure has not escaped the attention of that bastion of inflation-fighting, the Federal Reserve. In the past two beige books, the Fed's roundup of regional economic activity, the central bank has noted the spot shortages of skilled workers and the effect on wages.

REAL WAGES START GAINING GROUND



One result of this imbalance is that average wage growth is outpacing inflation. Using the Commerce Dept.'s new chain-weighted price index for consumer spending, real wages have been increasing steadily since 1993 (chart). The index is a better cost-of-living measure than the consumer price index because it is not based on a fixed basket of items but allows for changes in spending patterns.

THE CLEAR UPTREND in real wages, along with profit growth that has gone from spectacular to still respectable, all within a period of low inflation, seem at odds with each other. Usually this far into an expansion, these trends begin to fight each other. Higher productivity growth is about the only explanation for this ongoing harmony.

That's why the Labor Dept.'s recent downward revision to productivity growth seems so counterintuitive. The new data on output per hour worked in the nonfarm sector, which currently run through the third quarter of last year and mainly incorporate the Commerce Dept.'s chain-weighted measure of national output, show productivity growth in this expansion of only 1.4% per year, vs. 2.2% for the old data. That's well below the average pace for recent expansions. More startling, productivity growth over the past two years, using the new numbers, drops to a mere 0.9%, from the 2.6% originally thought (chart, page 28).

The key implication here for the inflation outlook is that the annual pace of nonfarm unit labor costs, instead of rising 0.3% over the past year, as the old data showed, is now reported to have increased by 3%,

and that 3% is a steady acceleration from a 1% annual growth rate a year earlier. In the old data, the pace of unit costs had been lounging generally below 1% for the past two years.

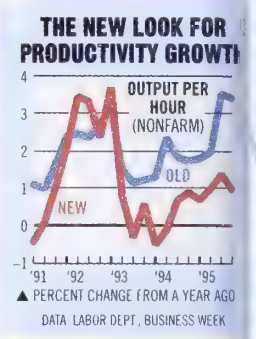
Unit labor cost, which is the cost of producing each unit of output, acts like a floor under prices. The new productivity numbers suggest that, despite still-modest growth in wages and benefits, there's more inflation potential in the labor markets than the old data implied.

THE PROBLEM SEEMS TO EXIST more in the productivity data than it does in reality. The new chain-weighted output numbers will probably be shown to understate output growth when Commerce makes further revisions later this year, and even then, productivity in services remains extremely difficult to measure.

For example, one little-recognized statistic from the productivity revisions is that, during this expansion, productivity in the manufacturing sector, where output is easy to count, was actually revised slightly higher in the new data—3.5% per year, vs. 3.4%. But it was the factory sector that took the biggest hit in the downward revision to output. As a result of still-strong productivity growth, unit labor costs in manufacturing are actually falling.

One thing that the factory productivity data ignore, however, are the shifts in today's labor force. Hou worked in the factory sector are probably understat because the total does not include the thousands temporary or contingent workers who are on the f tory floor but not the factory payroll. Instead, the workers are considered employees of temporary-he agencies, which Labor classifies as a service indust

That and other measurement problems are reasons to question the implication that service-sector productivity during this upturn appears to have grown at an annual rate of little more than 0.6%. That result hardly seems believable, given the technology-driven substitution of capital for labor in various service-sector industries.



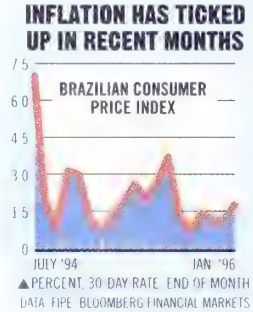
Technology can only go so far toward getting t product out, though. Businesses need knowledgeab workers to understand and run the sophisticated m chinery appearing in offices and factories today. this late stage of the expansion, companies will have be willing to shell out more money for scarce, hig tech skills. But if the result is greater productivit bigger paychecks will not automatically trigger hig er inflation.

BRAZIL

NOW THE FOCUS IS ON FISCAL REFORM

Thanks to a tightfisted monetary policy, Brazil's once-surging economy is coming in for a soft landing, but the challenge of fiscal reform remains.

After the 1994-95 flood of domestic demand and consumer credit, the economy appears ready to settle into a period of moderate growth, with a stable currency and lower inflation. A recent survey of 29 Brazilian financial institutions put 1996 growth in the 2.5%-to-4.5% range, compared with 4.2% in 1995 and nearly 5.7% in 1994. The currency, now at 0.97 reals per U.S. dollar, should end the year between 1.03 and 1.10.



Inflation will edge lower, the analysts say, to a 13%-to-17% range, vs. about 20% in 1995. The monthly inflation rate in January jumped to 1.82%, from 1.21% in December, as a result of one-time shocks (chart). But by early February, the 30-day rate had fallen back to 1.16%.

Fiscal reform, however, is the key to keeping inflation down, thus allowing for lower interest rates and a stable real. Reform efforts now target the costly pension system. Even tougher battles await for taxes, civil service, and labor laws. President Fernando Henrique Cardoso must move reforms through congress by midyear, even as the political agenda focuses on October's municipal elections. And he must convince the public sector that wages and inflation are truly delinked, all while maintaining a stable monetary policy.

Partly to that end, the central bank on Feb. 8 restricted the inflow of "hot money" that was pulled in by Brazil's 30% interest rates but was inflating the money supply. The bank levied a 5% tax on privatization funds set up to buy shares of state-run companies, banned these funds from investing in dollar-linked securities, lengthened maturities on bonds sold abroad, and opened up real estate and small companies to foreign investment. The aim: to redirect capital to more productive investments.

The problem is that these controls do not attack the underlying cause of such potentially destabilizing inflows—the current conflict between an ultratight monetary and an out-of-control fiscal policy.

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PRIMARIES

BASHING BIG BUSINESS

Corporate America is at the center of a split within the GO

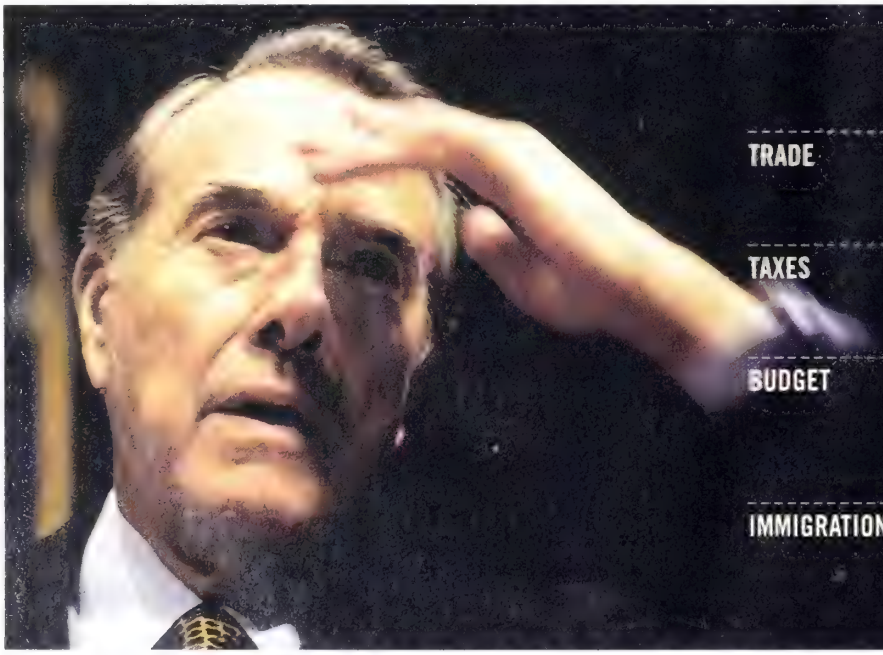
Ostensibly, the Republican candidates' slog through New Hampshire's snowdrifts is about the business of picking a Presidential nominee. But increasingly, the GOP's arduous nominating process—which kicked into high gear with the Feb. 12 Iowa caucuses—has evolved into a bitter struggle over the future direction of the Republican party itself.

On one side: an entrenched old guard with strong ties to Corporate America and pragmatic GOP elected officials. On the other: fiery populists who combine unyielding social conservatism with an economic nationalism that savages Wall Street and Washington alike. Their champion, riding the crest of a second-place finish in Iowa, is conservative commentator Patrick J. Buchanan, a well-heeled working-class hero with a penchant for bashing "the big boys in New York" who "don't give a hoot what the common people want." Also exploiting the anti-Establishment tide are two self-styled Washington outsiders, former Tennessee Governor Lamar Alexander and magazine publisher Steve Forbes.

At the moment, though, it's Buchanan who is surging. His low-budget, fiercely ideological campaign has ignited a grassroots insurgency that is weakening Establishment pillar Bob Dole's grip on the nomination. If there was any doubt about how big the chasm has grown, Iowa's caucuses told the tale. Dole eked out only a 26% victory, compared with the 38% of the vote he managed to pull in 1988. In a contest polarized along economic lines, Dole was favored by the wealthiest voters, while Buchanan led 29% to 24% among those earning less than $30,000 a year. And Buchanan's support from religious conservatives pushed him to within three percentage points of Dole, a showing he spun in the moral equivalent of victory.

As a result of Buchanan's right u percut, Dole's dreams of a quick victo are fading. He may have to endure lengthy state-by-state battle for de gates—the kind of grinding war of att tion that has President Clinton's adv ers feeling smug. "It's fascinating watch the Republicans disemboweli themselves," grins Senator Christoph J. Dodd (D.-Conn.), general chairman the Democratic National Committee.

The smiles don't stretch to Americ corporate suites, however. Big Bu ness has bet heavily on Do "Buchanan's views are worrisome," sa Bruce D. Cowen, president of TRC Co a maker of environmental equipme based in Windsor, Conn. "Without fr trade, our economy will hit a wal GOP heavyweight Richard B. Chen now chairman of Dallas-based Hallibu



DOLE'S TRADITIONAL REPUBLICAN STANDS...

TRADE	A NAFTA and GATT supporter, Dole now urges caution on new trade pacts
TAXES	Wary of a flat tax and its reven consequences, Dole promises explore a single-rate tax
BUDGET	An ardent deficit-cutter, the Se Majority Leader favors a consti tional amendment requiring a balanced budget
IMMIGRATION	On the stump, Dole supports o modest and temporary restrain legal immigration

Co., says Buchanan's doctrine is a
of latter-day "Know-Nothingism"
charges that his conspiratorial iso-
nism "appeals to the worst in-
ts in our society."

NEGATIVE. Dole, his party's Great
promiser, is viewed with suspicion
is rivals in the race and also by
line GOP freshmen. Still,
emains the overwhelm-
choice of executives,
value his skills as one
e capital's supreme leg-
ive tacticians. Trouble
Dole's mastery of a
hington system that
y voters see as hope-
y corrupt has become
of his biggest negatives, ranking
gside his muddled message.
hat's particularly worrisome for
y members of the boardroom set,
gh, is Buchanan's skillful manipula-
of populist resentment. With his
ing attacks on corpocrats who "ex-
American jobs abroad" and sign
ious free-trade pacts with shad-
foreign elites, Buchanan's America

ELECTION '96

In states with populist leanings, Buchanan could incite a backlash against decades of downsizings

Buchanan will get the chance to send more shivers down other CEOs' spines now that he is focused on New Hampshire and beyond. Although he lacks Forbes's megabucks and Dole's links to popular New Hampshire Governor Steve Merrill, Buchanan has always been popular with the state's gun owners and antitax activists. Buchanan also is backed by the influential *Manchester Union Leader*, a beacon of right-wing opinion. These assets clearly worry moderate business leaders. "Buchanan is in tune with the far right," frets Fred Bramante, CEO of Daddy's Junky Music Stores, a New England-based music retailer. "It will be a Clinton landslide if he's the nominee."

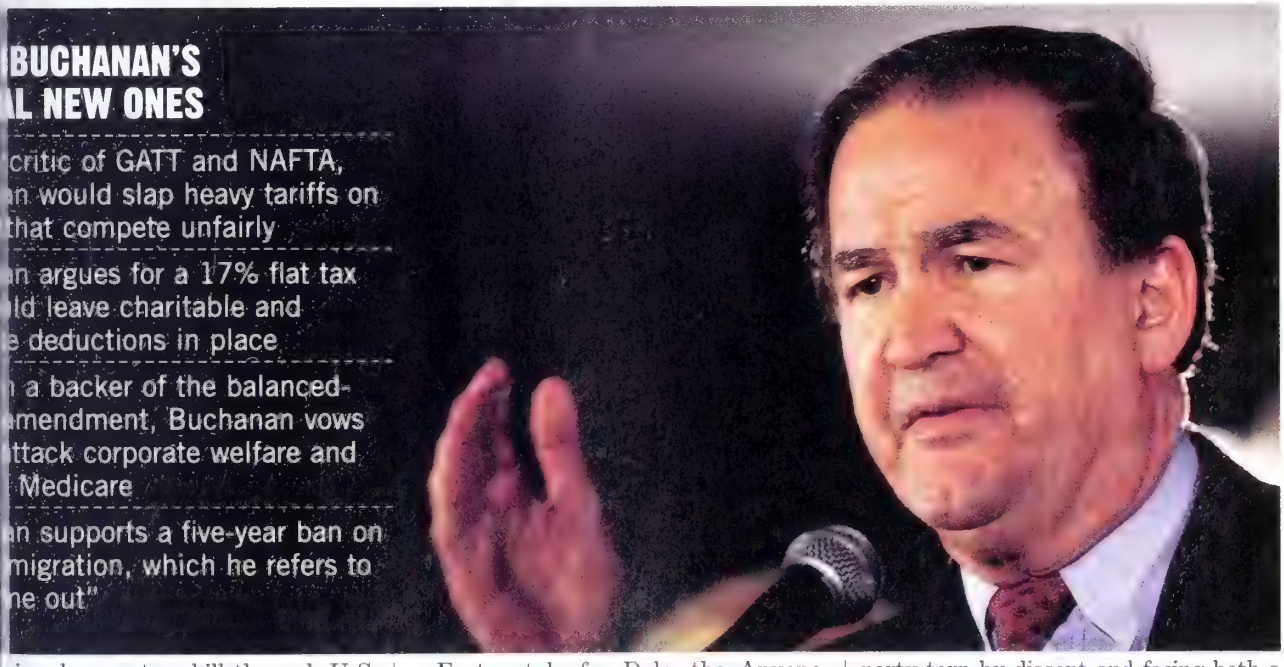
pronounced populist or fundamentalist leanings.

To repel the populist revolt, Dole is counting on GOP elected officials. Some 24 of the nation's 31 Republican governors have endorsed him, along with many top state legislators. The payoff, Dole reckons, will come in New York, the Midwest, and California. In the end, he's betting that rank-and-file Republicans won't be able to stomach the fiery Buchanan.

MORE CRITICS. He may be right. Polls show that Buchanan, even as he surges, has more critics within his party than admirers. Any Dole collapse, veteran pols believe, would be likely to drive voters toward the less polarizing Alexander. Even if Buchanan falls short, however, the anti-Washington, anti-Wall Street current he is riding could alter the Republican political landscape for years to come.

Somewhere along the line, Republicans will come together long enough to pick a standard-bearer. But with the party torn by dissent and facing both a bitter nominating struggle and a convention confrontation between its feuding factions, some GOP elders are beginning to wonder whether the nomination fight will position the party for national dominance—or give Bill Clinton another ticket to the White House.

By Lee Walczak in Washington and Richard S. Dunham in Des Moines, with Susan B. Garland in Washington and Gary McWilliams in Houston



BUCHANAN'S L NEW ONES

critic of GATT and NAFTA, n would slap heavy tariffs on that compete unfairly

n argues for a 17% flat tax ld leave charitable and e deductions in place

a backer of the balanced- mendment, Buchanan vows ttack corporate welfare and Medicare

n supports a five-year ban on migration, which he refers to he out"

ism has sent a chill through U.S. inationals. Globally-minded execs the type of protectionism es- ed by Buchanan as a dangerous of nostalgic yearning at best— nativist rabble-rousing at worst. s nation cannot return to isolation- says Stanley C. Gault, chairman oodyear Tire & Rubber Co. "In g so, we would allow the rest of world to pass us by."

ault expects protectionist argu- s to fall of their own weight. But

Fortunately for Dole, the Anyone-But-Bob vote is still split. Alexander placed third in Iowa and won a shot at becoming a real contender. Forbes is hoping that a boundless checkbook and fervently antitax Granite Staters will help him overcome his Iowa meltdown. His capitalist tools of choice: a 17% flat-tax proposal and an unlimited media budget to beam his "hope, growth, and opportunity" gospel to voters. Meanwhile, Buchanan is angling for March breakthroughs in Southern states with

CANDIDATES

THE CAPITALIST WALLFLOWER

Steve Forbes is a gutsy candidate but a timid investor

NO GO-GO Forbes, at a New York debutante party, invests much like a typical wealthy Easterner—complete with tax-dodging gentleman farm

Voters are beginning to learn something about Steve Forbes, the GOP's flat-taxing, supply-sider Presidential candidate. But what about Forbes the investor? With an estimated net worth of $440 million, Forbes registered the most extensive holdings in the financial disclosure reports required by the Federal Election Commission and filed by all candidates last year.

ELECTION '96

BUSINESS WEEK asked four seasoned financial planners to examine his portfolio. The big surprise: Forbes, editor-in-chief of a magazine that reveres the entrepreneur and often focuses on fast-growing midsize companies, isn't following his own advice. "He just doesn't buy the kinds of things that *Forbes* magazine writes much about," says Harold R. Evensky, of Coral Gables, Fla., who examined the report. Forbes likes "mostly stodgy old industries" such as utilities.

Forbes's biggest holding is his inherited 35% stake (he got 51% of voting shares) in Forbes Inc., the family business. Its worth, according to widely reported estimates: $407 million. CEO Forbes was required by the FEC report only to estimate the value of his patrimony as "over $1 million." Forbes's house and farm in Bedminster, N.J. add an estimated $26.5 million to his net worth. Stocks, bonds, real estate, and gold make up the rest—between $2.6 million and $7.5 million, the FEC filing says. It puts his pay at $775,000 a year.

For a man willing to spend "whatever it takes" in a kick-your-shins campaign, Forbes turns cautious when he invests. Half his personal fortune is buried in real estate. Nearly 30% is in domestic stocks and mutual funds—almost all load funds. Individual domestic shares are concentrated in utilities (35%), banking (23%), and insurance (17%).

For some excitement, Forbes generally looks abroad. He reported $300,000 to $600,000 worth of Teléfonos de México stock, and he has owned telephone stock in the Philippines, Argentina, and Spain. That's a clever way to invest in emerging markets, since such countries first must modernize telecommunications.

As if his flat-rate tax proposal weren't evidence enough, Forbes's portfolio also stresses his discomfort with taxes. No oil and gas limited partnerships, but there are a few tax-free municipal bonds. And he h[a]s a tiny livestock op[e]ration on his 500 a[c]res that generated $9,100 in profits [t]o justified a far la[r]ger farm-property abatement.

Forbes didn't h[a]ve to reveal any as[s]et sales that lost m[o]ney in his FEC fil[i]ng. His biggest cap[i]tal gains—as much a[s] $1 million—came from sales of the Mex[i]can telephone stock. But there are s[o]me hints that a few deals went bad. For[b]es had the misfortune of investing fa[r] money in the Washington Public Po[w]er Supply "Whoops" bonds that went [i]nto default in the mid-1980s. Their va[l]ue today is mainly as historical artifact[s].

PRIME CREDIT. Financial analysts ge[n]erally give Forbes high marks for stay[i]ng away from the riskier plays sugges[t]ed by articles in *Forbes* magazine. With[o]ut much in Forbes Inc., he's better off [d]iversifying, they argue. And as editor-[i]n-chief of a financial magazine, "the po[t]ential for conflict of interest there is [s]o great that he's better off in those mu[t]ual funds," says Martin Jaffe, CEO [o]f Wood, Struthers & Winthrop in N[e]w York, who also looked at the report.

Forbes receives praise for leveraging his portfolio with debt—not for [h]is campaign, which he has lent more t[h]an $14 million, but by borrowing aga[i]nst his farm. The documents show four-[a]nd-a-year mortgage loans in excess of $3 [m]illion at interest rates of 6.75% to 7.1[2]5%. So good is Forbes's cr[e]dit that he could bor[r]ow $500,000 to $1 mil[l]ion from the Bank of N[e]w York at prime.

It may surprise so[m]e that Forbes isn't a m[o]re exciting investor. But [o]ther than his political [i]nstinct for the jugular—[h]e has invested much of [h]is campaign money in ne[g]ative advertising—he p[r]efers to be known as [t]he Sam Walton of W[a]ll Street, driving his Bu[i]ck station wagon aro[u]nd Bedminster, 100,000 m[i]les on the odometer. Mo[s]t experts agree: Forbes's political campaign is l[i]kely to go down as his m[o]st investment yet.

By Paul Magnus[o]n in Washington

CANDIDATE FORBES: A STOCK PORTFOLIO

American Intl. Group
Teléfonos de México
Federal Home Loan Mortgage
Chemical Bank
Bank of New York
Chase Manhattan
Citicorp
Merck
AT&T
Bell Atlantic
American Express
Intel
Microsoft

DATA: FEDERAL ELECTION COMMISSION

DEREGULATION

OPERATOR, PLEASE CONNECT ME

Long-distance companies hunt for allies in the telecom wars

AT&T

•The nation's largest phone company is in preliminary talks with **MCI** to jointly build several local-calling networks.

AT&T has also signed 20 contracts to resell local capacity from competitive-access providers such as **MFS Communications**.

MCI

•Apart from any deal with **AT&T**, **MCI** has already agreed to purchase and resell cellular calling services from a number of providers, including **AT&T**. **MCI**, which is 20% owned by **British Telecommunications**, recently bought a cellular reseller, **Nationwide Cellular Service**.

MCI would be a natural partner for a Baby Bell.

Sprint

•**Sprint** has a joint venture with cable outfits **TCI**, **Comcast**, and **Cox** aimed at bundling long-distance, local, and cable-TV services. The four also are teaming up to sell wireless services under the **Sprint** brand name. Meanwhile, **Sprint**, 20% owned by **Deutsche Telekom** and **France Telecom**, is spinning off its cellular business.

WORLDCOM

•The nation's fourth-largest long-distance carrier has just signed deals to resell its service to **Ameritech** and **GTE**. Since **WorldCom** can offer the same nationwide coverage as the Big Three, more Bells are likely to flock to it—or even buy it—rather than give their business to **MCI**, **AT&T**, or **Sprint**.

LCI International

•**LCI**, the fifth-ranked company, has snagged the **Bell Atlantic-Nynex** cellular partnership, which will resell its long-distance service.

Like **WorldCom**, **LCI** is a natural merger partner for a Bell looking for a national long-distance network.

DATA: BUSINESS WEEK, COMPANY REPORTS

When such bitter rivals as AT&T and MCI Communications Corp. start talking alliance, it's clear that there's a whole new ball game in telecommunications.

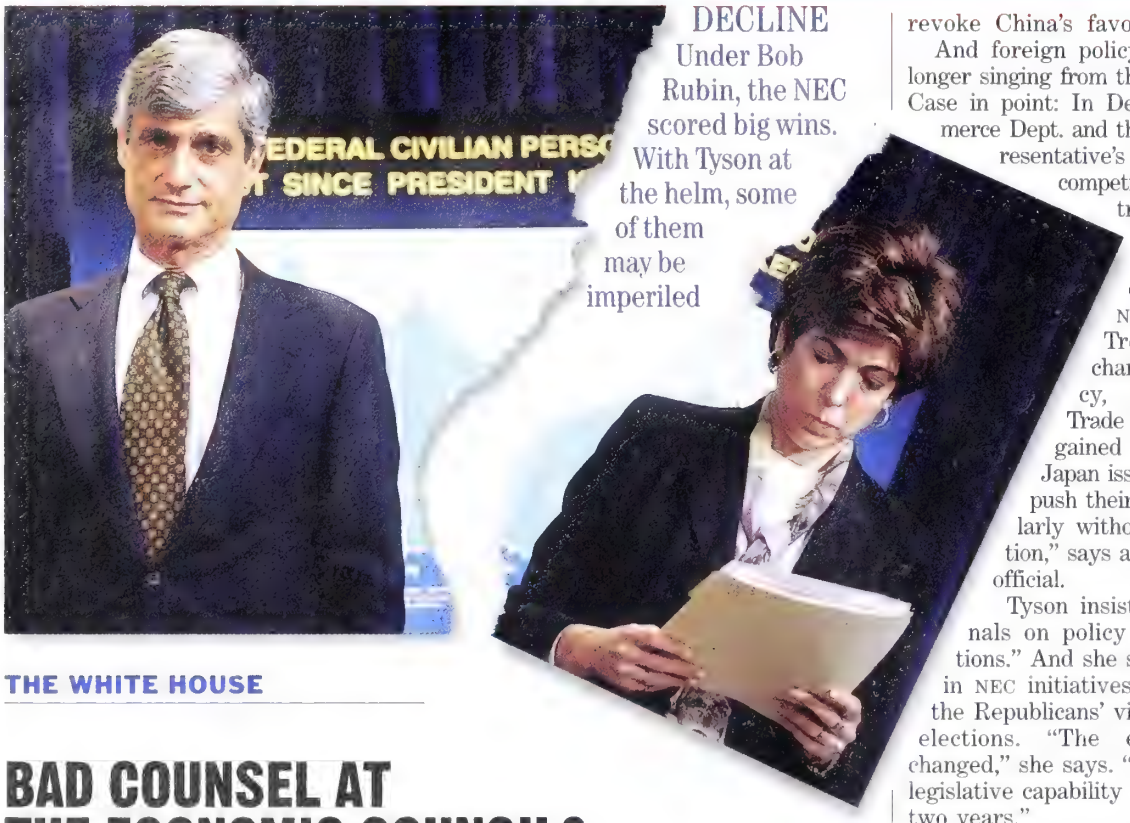
Since Feb. 8, when President Clinton signed legislation deregulating the business, the major long-distance carriers have been moving to establish themselves in the local, cable-TV, and other markets from which they had been barred. The initial goal is to offer local calling as the linchpin to a raft of services, from wireless to satellite TV. MCI CEO Bert C. Roberts Jr. has already let slip that his company is holding preliminary talks with AT&T. Their aim: to share the cost of building local-calling networks. For its part, AT&T has signed some 20 deals with rivals of regional Bell companies to resell local service, while Sprint Corp. and its cable partners are building a nationwide wireless network to be used for local access.

Don't expect any megamergers soon, however. For now, the long-distance carriers will initiate low-risk partnerships rather than high-risk acquisitions, testing the waters in new markets before making major financial commitments. Look for AT&T, MCI, and Sprint to sign resale agreements with Bell companies rather than merge with them. "There are a lot of paths to the customer, and it's a little early to declare exactly which one is the right one," says Joseph P. Nacchio, executive vice-president of AT&T's consumer and small-business division. So AT&T, MCI, and Sprint are seeking partnerships with any company with a wire into homes—from cable-TV operators to electric utilities.

TRUSTBUSTER ALERT. Besides, mergers may not be looked on kindly in an industry where the Big Three still hold a lock on the long-distance market. "Anytime there is a merger in this business, it gives the Justice Dept. a chance to sink its teeth into you," says Scott Cleland, an analyst with Washington Research Group, a consultancy. And Justice would likely come down hard on any deal that smacks of reconstituting the Bell System after all it went through to break up AT&T 11 years ago.

For smaller long-distance carriers, though, mergers could well be in the offing. WorldCom Inc. and LCI International Inc., the fourth- and fifth-largest long-distance carriers, are the partners of choice for the Baby Bells, which want to avoid giving business to their biggest rivals. A Baby Bell could acquire WorldCom or LCI and immediately vault into a top spot in the industry. That's one way to hit a home run in this brand-new telecom game.

By Catherine Arnst in New York, with bureau reports



DECLINE Under Bob Rubin, the NEC scored big wins. With Tyson at the helm, some of them may be imperiled

THE WHITE HOUSE

BAD COUNSEL AT THE ECONOMIC COUNCIL?

The "Felix Flub" is only the latest misstep

Felix G. Rohatyn's decision to withdraw as a candidate for vice-chairman of the Federal Reserve was a blow to President Clinton. But Rohatyn's Feb. 12 exit was even more embarrassing for Laura D'Andrea Tyson, director of the National Economic Council. Tyson headed the team responsible for vetting Fed nominations. Yet she failed to anticipate the fierce Republican opposition that prompted the 67-year-old Lazard Frères & Co. banker to back out. Now, the Administration is back to square one in trying to fill the vacancy.

The Felix Flub is the latest in a string of missteps that has some in Washington wondering: What's wrong at the NEC? In 1993, Clinton established the council, with Robert E. Rubin as its director, in order to elevate economics in policymaking and ensure that the Administration speaks with one voice on complex economic issues. In its early days, the NEC racked up a string of highly visible successes—from shepherding the 1993 deficit-reduction package through Congress to persuading lawmakers to delink China's most-favored-nation trade status from its human rights record. "The NEC is one of the most important innovations of the Clinton Administration," says Commerce Secretary Ronald H. Brown.

Increasingly, though, the agency is failing to forge consensus. Take present Treasury Secretary Rubin's November trip to Argentina. Rubin planned to complain to President Carlos Menem about Argentina's failure to protect U.S. trademarks and patents. But the Treasury chief was stunned to learn on his arrival that U.S. Trade Representative Mickey Kantor had preempted his quiet diplomacy. In a letter to the Argentines that arrived ahead of Rubin, Kantor rebuked Argentina for lackluster enforcement of intellectual property rights. The NEC is supposed to prevent such confusion, but "the letter wasn't cleared," says Tyson. A Rubin aide says the timing was unfortunate. Kantor declined to comment on the letter.

"RARE EXCEPTIONS." Now, even some of the NEC's early accomplishments are starting to fray. U.S.-Japanese policy—once a Clintonite obsession—is in the doldrums. Expansion of the North American Free Trade Agreement to Chile and the rest of Latin America is stalled. Congress is once again threatening to revoke China's favored trade stat

And foreign policy agencies are longer singing from the same hymnbo Case in point: In December, the Co merce Dept. and the U.S. Trade R resentative's Office clashed o competing plans to enfo trade pacts. All su disputes sho be brokered a eliminated by t NEC. Under Rub Treasury has tak charge of Mexico p cy, while the U Trade Representative l gained the upper hand Japan issues. "Agencies n push their own policies re larly without much coordi tion," says a former U.S. tra official.

Tyson insists that mixed s nals on policy are "rare exce tions." And she says any slowdo in NEC initiatives is largely due the Republicans' victories in the 19 elections. "The environment h changed," she says. "We don't have t legislative capability we had in the fi two years."

Tyson has a point. In the balanc budget fight, the White House w forced to play defense and the NEC v tually disappeared from view wh Chief of Staff Leon E. Panetta direct maneuvers. Behind the scenes, howev Tyson helped shape strategy.

With Rohatyn, though, the N has suffered a highly visible defe Tyson never saw that the GOP-r Senate Banking Committee would hostile to a nominee with Rohaty advocacy of government activi and economic stimulus that might bo inflation.

Recently, Tyson has moved strengthen the NEC's hand. She has stituted weekly meetings with Cabi officers responsible for internatio economics. She also reorganized h aides to better manage the thi staffed agency. On Capitol Hill, Sena Ernest F. Hollings (D-S.C.) and oth Democrats hope to bolster the ager with legislation to write the NEC a its role into law. That way, t NEC won't die after Clinton's Presid cy ends.

But survival isn't enough. Unl Tyson can end the flubs and return t council to its former stature, the N may live only as another Clinton-e monument to good intentions.

By Amy Borrus and Mike McNam in Washington

COMMENTARY

By Owen Ullmann

THE 'GLASS CEILING' IN THE CABINET ROOM

What do Alice M. Rivlin, Donna E. Shalala, Janet Reno, Hazel R. O'Leary, Carol M. Browner, and Laura D'Andrea Tyson have in common? Sure, all are accomplished women who hold top-level jobs in the Clinton Administration. But they also have something else in common: None seems to wield the same influence as her male predecessor or counterpart in the Administration.

Call it President Clinton's new woman problem. Although he has placed far more women in Cabinet-level jobs than any previous Chief Executive, the President nonetheless seems most comfortable governing with the help of an inner circle of male counselors. The sole exception is First Lady Hillary Rodham Clinton. Otherwise, laments one senior female official, "there's the boys' team and the girls' team. It's sad but true." Another top woman says the bias is subtle. "We're in the room, treated with respect, and listened to. I just don't think our ideas carry as much weight."

Consider the lot of Rivlin, the director of the Office of Management & Budget. If she had her druthers, friends say, she would have led the way to a compromise balanced-budget plan with Capitol Hill Republicans. But White House budget strategy was commandeered by Chief of Staff Leon E. Panetta, Rivlin's predecessor at OMB. Panetta's political skills were considered more vital than Rivlin's fiscal acumen.

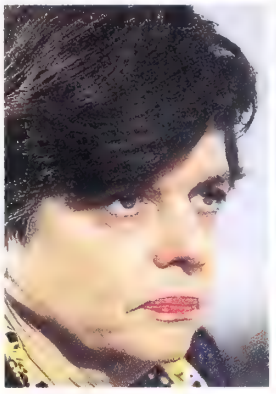
MERE VISIBILITY." Then there's Health & Human Services Secretary Shalala, who lost control over the biggest policy issue involving her agency: health-care reform. That project was managed from inside the White House by adviser Ira C. Magaziner—working with Hillary Clinton, not Shalala.

At the Justice Dept., Clinton's maverick Attorney General, Janet Reno, is in charge of law-enforcement issues. But she does not serve as a Presidential confidante on legal matters, as have most of her male predecessors. Energy Secretary O'Leary was derided by White House officials as a nonplayer long before she recently embarrassed the Administration with a flap over her extravagant travel budget. Browner, head of the Environmental Protection Agency, doesn't set EPA policy—that's done, some Clintonites say, by her mentor, Vice-President Al Gore. Tyson, director of the National Economic Council, doesn't appear to have as much clout as her male predecessor, Robert E. Rubin, who is now Treasury Secretary.

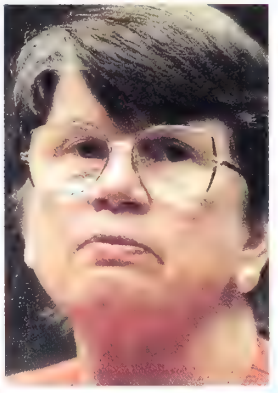
'THE GIRLS' TEAM'

"We're in the room, treated with respect, and listened to. I just don't think our ideas carry as much weight" as those of men like Rubin and Panetta

HAZEL O'LEARY: *Energy Secretary*



ALICE RIVLIN: *OMB Director*



JANET RENO: *Attorney General*

And consider the plight of former Presidential press secretary Dee Dee Myers, who resigned because she was denied the close access to Bill Clinton enjoyed by both her predecessor, George R. Stephanopoulos, and successor, Michael D. McCurry. Ross K. Baker, a Presidential scholar at Rutgers University, claims that Clinton's appointment of women to prominent positions "is a liberal attempt to go for mere visibility—gender diversity. But when you look deeper, you see there's not a lot of influence that goes with these jobs."

Clinton's defenders vehemently deny that the President is guilty of gender bias. "I have never felt that my advice is not heard," says EPA's Browner. Cabinet Secretary Kitty Higgins, the liaison between the White House and the agencies, declares: "There are more women in senior positions of influence in this Administration than any place I've ever seen." And HHS Secretary Shalala—leaving aside the handling of health-care reform—says that over the past two years, women have been dominant players in setting "all social and health-care policy" for the Administration.

Perhaps. But even Shalala concedes that she has women friends in the Administration who might disagree with her, although they won't do so on the record.

OUT OF THE LOOP. Some male counterparts speculate that these women aren't "political" enough and don't have the "sharp elbows" men have learned to use to get their way. And in some cases, the women in top posts are out of the loop because their male and female colleagues don't think they are up to the job. But some of Clinton's top men aren't such sharp operators, either. So it's hard to blame the problem solely on performance.

Whatever the source of their frustration, senior women who work for Clinton say they don't have the President's ear. It's a problem Clinton needs to fix. If he doesn't think his top women advisers are up to the job, he should replace them—and stop using them as diversity window dressing.

Ullmann is BUSINESS WEEK's Washington Senior News Editor.

AUTOS

WHAT FORD HAS RIDING ON THESE FOUR WHEELS

The hot '97 F-150 might provide the oomph the new Taurus hasn't

Frank Oberle likes the look and feel of a new pickup truck. That's why he has purchased four Dodge Rams since 1993. But as soon as the curvy new Ford F-150 hit town, Oberle traded in his trendy red 1996 Ram for a $28,000 burgundy F-150. "It's not as aggressive-looking as the Ram, but I'm getting a lot more comments on the Ford," says the 36-year-old food-factory machinist in Utica, N. Y. "It's the new thing."

Ford is counting on the reworked F-150 to haul in trend-followers such as Oberle as well as the usual hard hats and farmers. To do that—and break its string of sluggish new-model launches—Ford must also persuade traditional F-150 owners to accept the swoopy new styling and stiffer sticker price. So far, so good: Dealers have deluged Ford with 140,000 orders for the new model, which was only introduced on Jan. 25.

CASH COW. Success is critical to Ford. The F-series pickup cost $4 billion to redesign, churns out about $3,500 in gross profits per unit, and keeps six factories humming. And Ford badly wants the F-series to remain America's top-selling vehicle, racking up nearly 700,000 sales annually. "This truck is the single most important product for Ford in North America," says Schroder Wertheim & Co. analyst John Casesa. "The whole company is running on profits from the F-series and the Explorer."

To gain new converts, Ford is gunning for younger, more affluent buyers (table). That audience largely spurned the brickish old F-150 in favor of the 18-wheeler styling of the Dodge Ram or the smooth look of the Chevrolet C/K. Now, the aerodynamic new F-150 seems modern and is packed with car-style features such as an overhead-cam engine and a cushy suspension that rides like a sedan. Its new engine even runs 100,000 miles before its first tune-up, a feature usually found only on luxury cars. One good sign: The once utilitarian beast of burden is gaining a following in California's trendier areas. "People are buying this truck for the image—it's an extension of their personal wardrobe," says analyst Christopher W. Cedergren of AutoPacific Group Inc. in Santa Ana, Calif.

FOUR-BILLION-DOLLAR BABY: *Its first face-lift in 16 years wasn't cheap*

YUPPIFIED

How Ford expects the sales demographics of its F-150 to change

	OLD F-150	NEW F-150
MEDIAN AGE	44	39-42
COLLEGE GRADS	22%	30%
MEDIAN INCOME	$49,000	$50,000
PARENTS	34%	46%
EMPTY-NEST COUPLES	37%	27%

The F-150 is no bargain. Prices begin at $15,660—about $1,000 more than the Chevy and $1,300 more than the Dodge—and rise to more than $30,000. Ford expects its most popular model to be the F-150 XLT with an extended cab and automatic transmission. It starts at $22,581. But Ford contends the higher prices are offset by extra features such as dual air bags and a standard third door that opens to the rear seat or extended-cab version. Chevy charges $425 for its third door, and Dodge doesn't have one. "I don't mean to be arrogant," says Bobbie Gaunt, Ford's general marketing manager, "but I can't imagine what could go wrong with this truck."

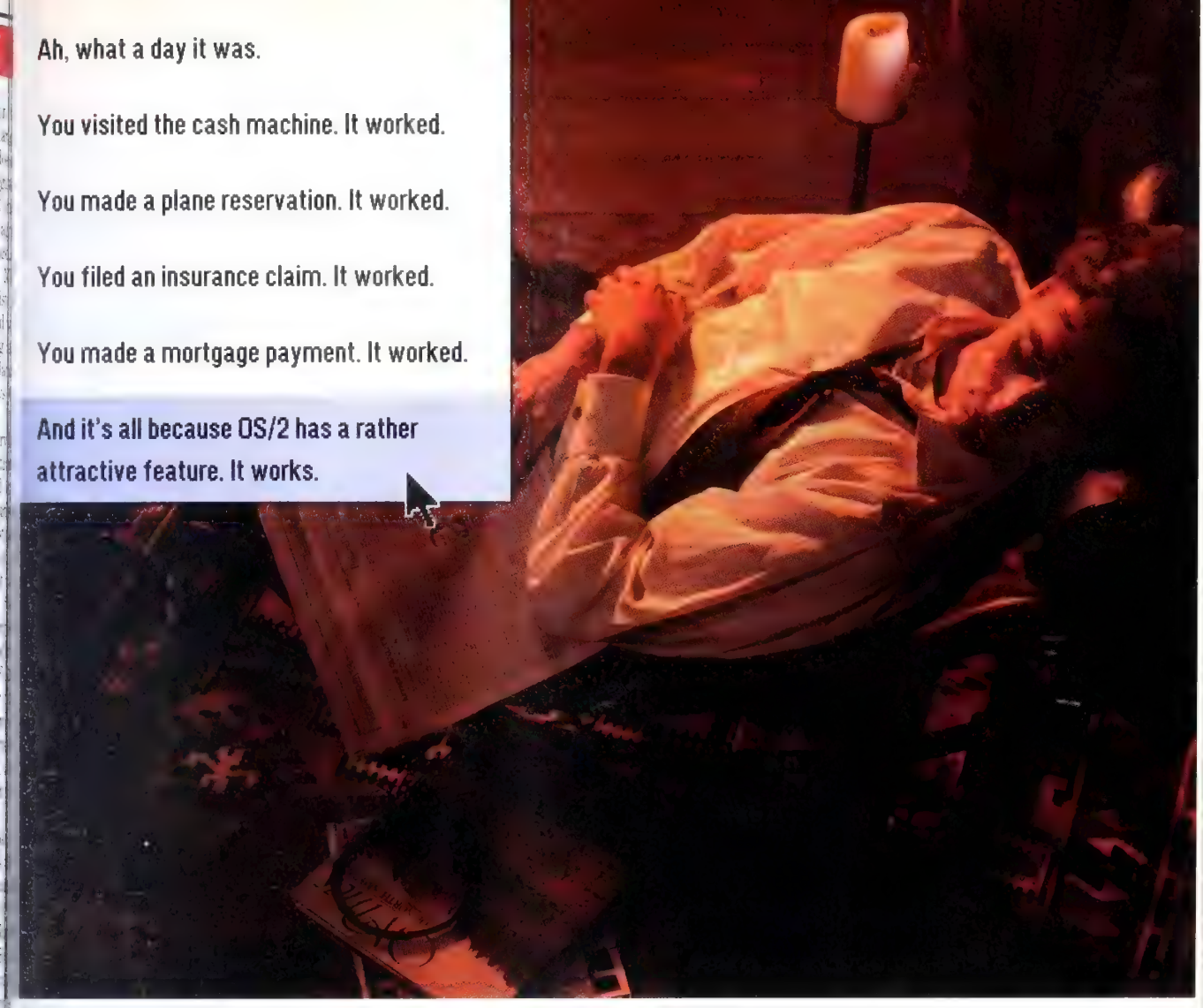
Fred Ostrick can. The retired New York fireman and truck traditionalist recently test-drove the new F-150 and was turned off by its "bulbous" styling and carlike ride. "If I wanted a sedan, I would go out and buy a sedan," says the trick, 60.

MELDED DESIGNS. But Ford is trying hard not to offend too many such traditionalists. It gave a not-too-radical look to the new F-150 by melding a futuristic design concept from its California studio with a more conservative one out of Detroit studio. It will hedge its bets further when it introduces updates of the heavier-duty F-250 and F-350 later this year. Those will have more boxy looks and a more rugged ride than the sculpted F-150.

Ford also took big chances with its $100 million ad campaign for the F-150, which debuted during January's Super Bowl broadcast. The campaign, Ford's largest ever for a truck, resurrected the "Built Ford tough" slogan and features leather—and camp—Hollywood cowboy John Palance riding high in an F-150. The company says the new wave of commercials, coming this spring, will have a softer theme, stressing features such as cup holders and air bags.

Ford is trying to strike a delicate balance with the F-150 launch because it is desperate for a hit. Both its Contour sedan and Windstar minivan had slow starts. Its new Taurus, which came out last fall, has been faltering, too. Ford had to slap $600 rebates on all these models to spur sales. "A lot of people felt the new Taurus was overpriced," says Robert C. Failing, a Ford dealer in St. Johnsville, N. Y. "But people are fighting the price of the F-series truck." If that enthusiasm holds, this is the Ford product launch that won't sputter at the starting line.

By Keith Naughton in Detroit



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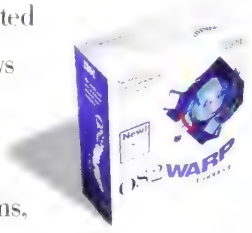

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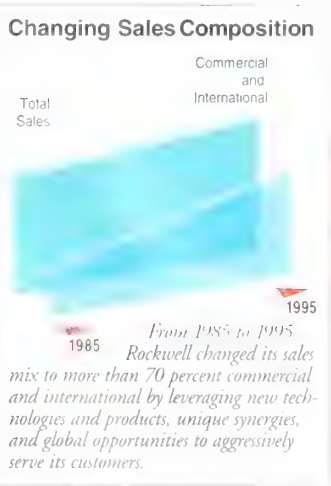

From 1985 to 1995 Rockwell changed its sales mix to more than 70 percent commercial and international by leveraging new technologies and products, unique synergies, and global opportunities to aggressively serve its customers.

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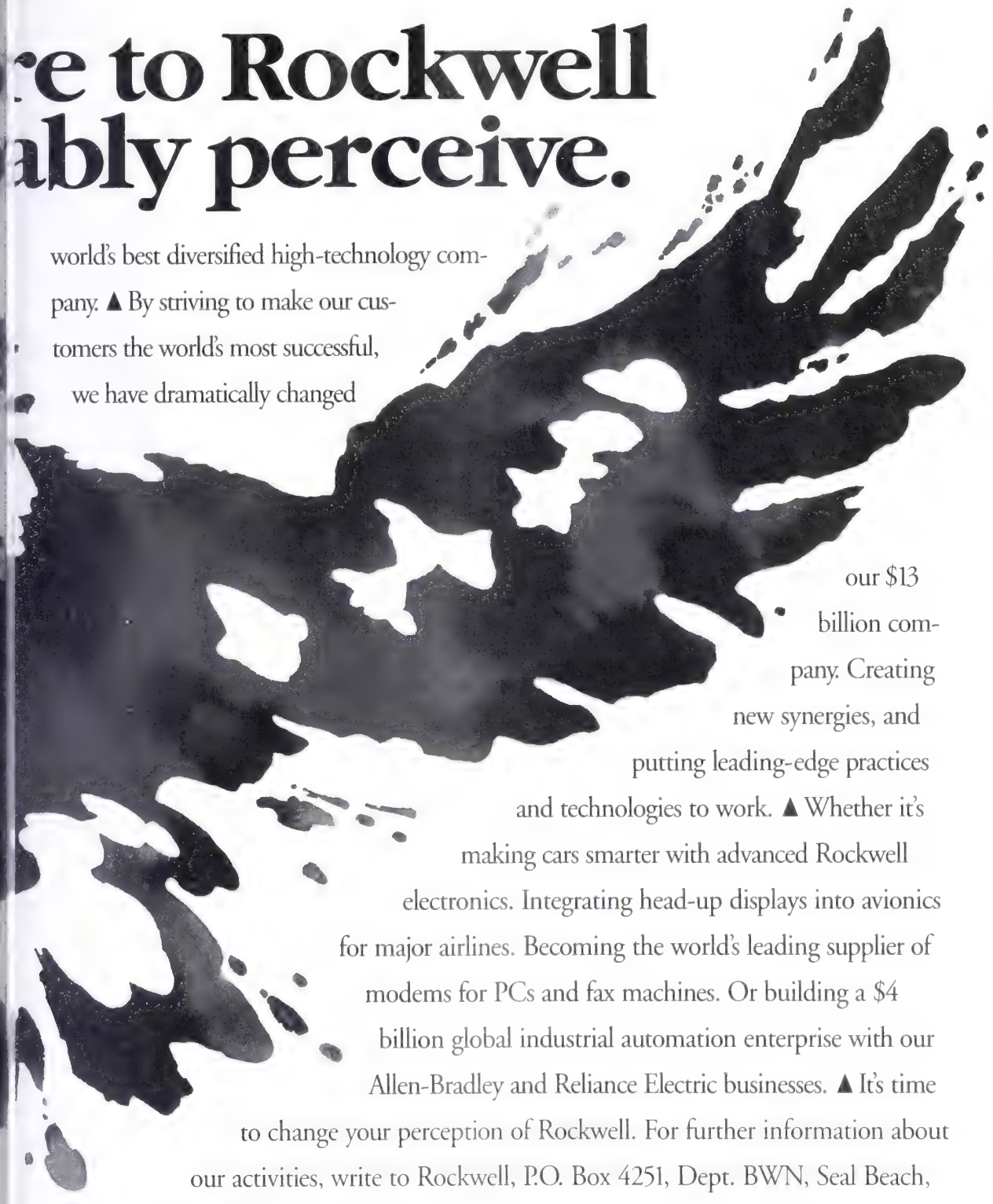

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STRATEGIES

H&R BLOCK MAY BE GOING OFF-LINE

A spin-off of its CompuServe unit seems to be in the works

For years, the Bloch family insisted that it made sense to keep H&R Block Inc.'s tax preparation unit paired with the booming CompuServe Inc. online network. The idea: Block could sell its tax services via CompuServe, and CompuServe could benefit from Block's cash and from its link to a well-known brand name. Trouble is, the synergies didn't add up to much. Now, Wall Street figures CompuServe would be worth a lot more on its own.

Richard H. Brown, who replaced Thomas M. Bloch as chief executive six months ago, appears about ready to go along with that idea. Investors think the former Ameritech Corp. vice-chairman, the first non-Bloch to lead the 41-year-old company, is prettying up CompuServe to do at least a partial sell-off of its shares. Block's share price is up more than 10%, to 38, since mid-January on the speculation, though it's still way below the 46¾ it traded at last November. "When they have the team in place, I think they'll spin it," says Bart Wear of Milwaukee's Firstar Investments, which owns 1.3 million Block shares. Brown was unavailable.

If that's what Brown is up to, it's a risky maneuver. Wall Street has long argued for a spin-off, figuring that CompuServe's valuation-per-subscriber would jump to about the level of rival America Online Inc. That would raise Block's and CompuServe's combined market capitalization about 19%, to $4.6 billion.

But a spin-off also might leave Block vulnerable if Congress ever passes a simplified flat tax, like the one backed by GOP Presidential candidates Steve Forbes and Pat Buchanan. Tax preparation will account for about half of the company's estimated $182 million in profits and $1.6 billion in sales in the fiscal year that ends Apr. 30—and profits are already relatively weak (chart). Many analysts figure Block could do well under a flat tax that maintains at least a handful of deductions because many people who now use costly accountants would turn to Block, whose average tax preparation bill is only $60. But if a flat tax were passed without any deductions at all, Block likely would be devastated.

A SEARCH. Nonetheless, signs are clear that Brown is preparing for big changes at CompuServe. He's building up its management, which analysts see as a sign that he's getting the unit ready to run itself. Recently, he started a search for a chief financial officer—a new post that would be important in selling shares to institutional investors. He is also hiring a new marketing chief at CompuServe and replacing its top European and consumer executives. And Goldman, Sachs & Co. is checking into selling a CompuServe stake to the public, according to a source close to the company. A spokeswoman says Block will consider all options to increase shareholder value but declined to comment specifically on a spin-off.

RISKY PLAY Without CompuServe, Block would be even more dependent on a business that could be shaken up by a flat tax

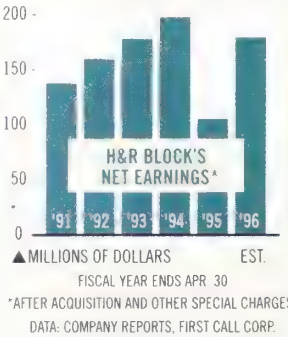
CompuServe could use a boost. Last year, it lost its place as the largest online service to upstart AOL. AOL tripled its subscribers, to 5 million, while CompuServe's base only doubled, to 4 million. Now, CompuServe is having to spend heavily to catch up. Analysts figure that it could cut its operating margins from 26% last year to 20% in the current fiscal year. More important, the rising popularity of the Internet's World Wide Web threatens to rob CompuServe of subscribers and content. "The content providers are all defecting to the Web because they don't want to be limited to the audience of one online service—and they want more control," says Mary Doyle, a senior analyst at the IDC/Link unit of market researcher International Data Corp.

One sign of the times: Just a year ago, content providers got only 20¢ of every dollar a subscriber spent looking at their product—CompuServe or AOL would keep the rest. Now, content providers get about 50¢ on the dollar.

CompuServe, meanwhile, is laying out big bucks to develop its own content and diversify its service. This month it launched its own Internet-only service called SPRYNET, which will give subscribers unlimited access to the Web for $19.95 a month. This spring, it plans to introduce wow!, an online service for computer novices. But pressure is growing for a spin-off. Risky as such a move might be, it would give Block lots of real cash—and earn it real kudos of goodwill on Wall Street.

By Peter Elstrom in Chicago

NOT-SO-HAPPY RETURNS



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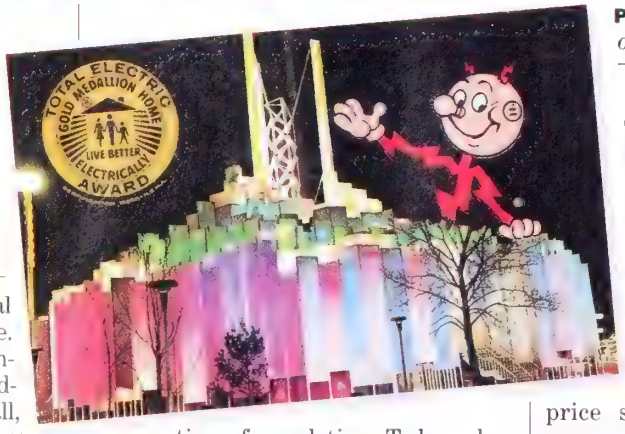
COMMODITIES

FUTURES SHOCK

Electricity contracts may help deregulate utilities



POWER ICON: *Reddy Kilowatt on a '64 World's Fair postcar*

Platinum futures, fine. Natural gas and crude-oil futures, sure. But is the New York Mercantile Exchange serious about trading futures in electricity? After all, the price of electricity has long been tightly regulated—and for the most part remains so.

No matter. Nymex is readying a new pit in downtown Manhattan that on Mar. 29 will begin trading in electricity futures, contracts that promise delivery of electricity at a specified price on a particular date. Sure, the introduction of many futures contracts has failed in the past. But experts say the market for electricity is large enough to eventually make these futures work.

The new contract is as much a political event as a financial one, because it could help finish off the last great bastion of regulation. Today, electricity prices are generally set by regulators. But market-based pricing is creeping in, mainly on sales between utilities. The Nymex move should increase interutility trading by making prices more visible.

WILD PRICE SWINGS. That's just the first step. Once utilities have free-market pricing, their customers will demand the same. Says W. Robert Parkey Jr., general manager of Aquila Power Corp., the unregulated power-marketing arm of UtiliCorp United Inc. in Kansas City, Mo.: "The whole regulatory compact is being thrown up against the wall."

While electricity rates customers have been genera stable, spot prices for utilit are extremely volatile. Becau brownouts and blackouts wr such havoc, utilities can't ford to delay purchases even five minutes in ho that prices will become m reasonable. Last summ when Chicago suffered a vere heat wave, the local s price spiked from around $20 megawatt-hour to as much as $1 says Shannon B. Burchette, senior vi president for marketing at Duke/Lo Dreyfus, a Wilton (Conn.) power m keter. Futures contracts should h utilities insulate themselves from w price swings.

Exchange President R. Patr Thompson says he hopes the electric futures contract will set a free-mark example that will hasten wider compe tion. If so, those guys in the funny ja ets may do more to change the utility dustry than a legion of bureaucrats.

By Peter Coy in New York, w Greg Burns in Chicago

EXECUTIVE PAY

AN INSANELY GREAT PAYCHECK

Is new Apple CEO Gil Amelio worth his millions?

Apple Computer Inc. has world-class problems. And now it has got a chairman and CEO who's pulling down a world-class pay package. Gilbert F. Amelio, a board member since late 1994, who took the helm on Feb. 5, will earn at least $2.5 million a year, according to Securities & Exchange Commission documents. And if he meets unspecified performance goals, the total package will be worth between $10 million and $13 million annually.

That doesn't quite make him a superstar among high-priced turnaround experts—but he is close. According to executive-compensation expert Graef Crystal, IBM chief Louis V. Gerstner Jr. earned $17.2 million in 1994, while AlliedSignal CEO Lawrence A. Bossidy took in $30.5 million. But Amelio stacks up better against the likes of Eastman Kodak CEO George Fisher, at $6 million. "He wouldn't make the finals of the biggest-pigs-in-America competition," says Crystal. "But these are high numbers."

Here's the nitty-gritty: Amelio will get $2.5 million in annual salary and guaranteed bonus, as well as a $5 million loan. The remaining 75%-plus of his possible pay is tied closely to Apple's financial health—in line with industry practices, analysts say. He will also get options to buy 1 million shares at the current market price. In addition, he has grants of up to 200,000 shares for each of the next five years, along w the potential for additional cash bonus for as much as $2.5 million more p annum. If Apple changes hands with the next year, Amelio gets a cool $ million.

"GETS WINDED." The question now whether Amelio, 52, will be worth t investment. Having turned arou Rockwell Corp.'s communications u and resuscitated National Semiconduc Corp., he clearly knows how to make impact. At Apple, he has already nix the quarterly dividend and moved squelch takeover rumors.

Over the long haul, though, Ameli track record is troubling. National Se conductor's stock has seriously und performed the s since last May, cording to Cryst "He's Mr. Bell-Shap Curve," Crystal sa "He's good at t 10-yard dash, b tends to get winde Given Apple's pr lems, the board h better hope Ame has developed so stamina.

By Peter Burro in San Francisco

GIL'S GELT
CEO Amelio's straight salary is $2.5 million. And if Apple changes hands within the next year, he gets a $10 million bonus

TED BY KELLEY HOLLAND

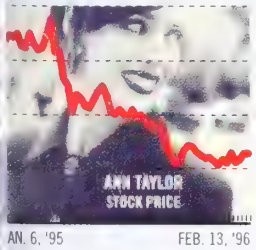
IEAT AND CHAFF CIGNA

NING A MAJOR ROUND IN A thy battle with its rivals, IA got the green light to its asbestos and environtal obligations from its perty-casualty business. n regulatory clearances in t states, the company on 12 set up an inactive unit $4.5 billion in assets to lle asbestos and environtal claims. CIGNA will back ith $800 million in reinnce, up from $500 million ally, plus an additional $50 on in payments over five s. The hefty collateral was anded by Pennsylvania ulators under pressure n rivals AIG, St. Paul, and bb. Those competitors will pressing to dismantle the plan. And Dow Chemical, Pfizer, and other policyholders plan to sue, arguing for some say before their policies get bucked to the new unit. CIGNA says regulators make such decisions, not policyholders.

CLOSING BELL

OFF TO ATNY

n Taylor Stores got badly ded management reincement on Feb. 9 when it ned J. Patrick Spainhour, na Karan's CFO, as its v president. Spainhour l be No. 2 to Ann Taylor Sally Frame Kasaks and l focus on operating probns. Ann Taylor's stock price s been falling for more n a year because of a kluster retail environment, clining same-store sales, l management depares. It pared back its exnsion plans just before the ainhour announcement.



AN. 6, '95 FEB. 13, '96

DATA BLOOMBERG FINANCIAL MARKETS

VALENTINE FOR HELENE CURTIS

SUAVE SHAMPOOS AND DEGREE deodorants attracted a Valentine's Day suitor. A U.S. subsidiary of Unilever PLC agreed on Feb. 14 to buy Helene Curtis Industries for a hefty $70 per share, or $770 million. Helene Curtis had traded as low as $27.50 last year. The announcement came a month after Roy Disney's Shamrock Holdings, which has a 7.6% stake in the company, called for a sale or restructuring. The founding Gidwitz family of Chicago has pledged its 75% voting shares to the deal. CEO Ronald Gidwitz will stay on.

WHY YOU'LL SOON HATE *TOY STORY*

AFTER UNDERESTIMATING THE demand for toys based on the animated film *Toy Story*, Disney is taking no chances with the Oct. 30 release of the movie's video. Accompanying the release will be a record $100 million marketing push, including 50 new toys or other merchandise—and Disney will have beefed-up licensing agreements on the stuff. Burger King, General Mills, and Kodak will also stage promotions. *Toy Story* has so far grossed over $180 million at the box office.

BLOOMBERG MEETS GUTENBERG

HIS NAME IS ALREADY flagged across TV broadcasts, radio shows, magazines, and on the Bloomberg data terminals dotting Wall Street trading floors. Now, Michael Bloomberg is turning to an older media: book publishing. This spring, Bloomberg will launch Bloomberg Press, which will publish books on personal finance for consumers and reference works for the finance and business types who are most of Bloomberg's customers. The first titles will be penned mostly by Bloomberg staffers and distributed by a subsidiary of Times Mirror. No word yet on the advances Bloomberg staffers can expect.

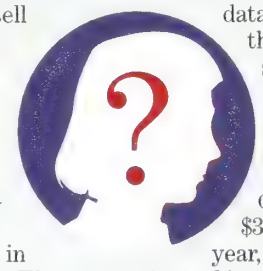
HELL WEEK AT RANDOM HOUSE

IF YOU THINK YOU HAD A BAD week, check out Random House. First, the New York publisher faced an avalanche of bad publicity on the news that it had pulled the plug on a book by performance artist Karen Finley. It was deemed too pointed a parody of books by domestic goddess Martha Stewart, a more influential Crown author. "This is not about money or publicity," says Finley. "It's about censorship and sexist views of women." Then, on Feb. 13, Random House lost a $1.3 million lawsuit against TV star and author Joan Collins. Random House says Finley, who gets to keep her advance, will benefit from the publicity but otherwise declined to comment.

HEADLINER: UNKNOWN

WANTED: ONE TOUGH TECHIE

General Motors is scouting for a new chief information officer. BUSINESS WEEK has learned that headhunters at Russell Reynolds Associates are beating the bushes for a computer honcho who could plot GM's technical strategy and look out for its interests in dealings with its Electronic Data Systems unit. A GM spokeswoman confirms the search, but won't discuss it. Scuttlebutt—denied by GM—is that the new job will pay up to $1 million.

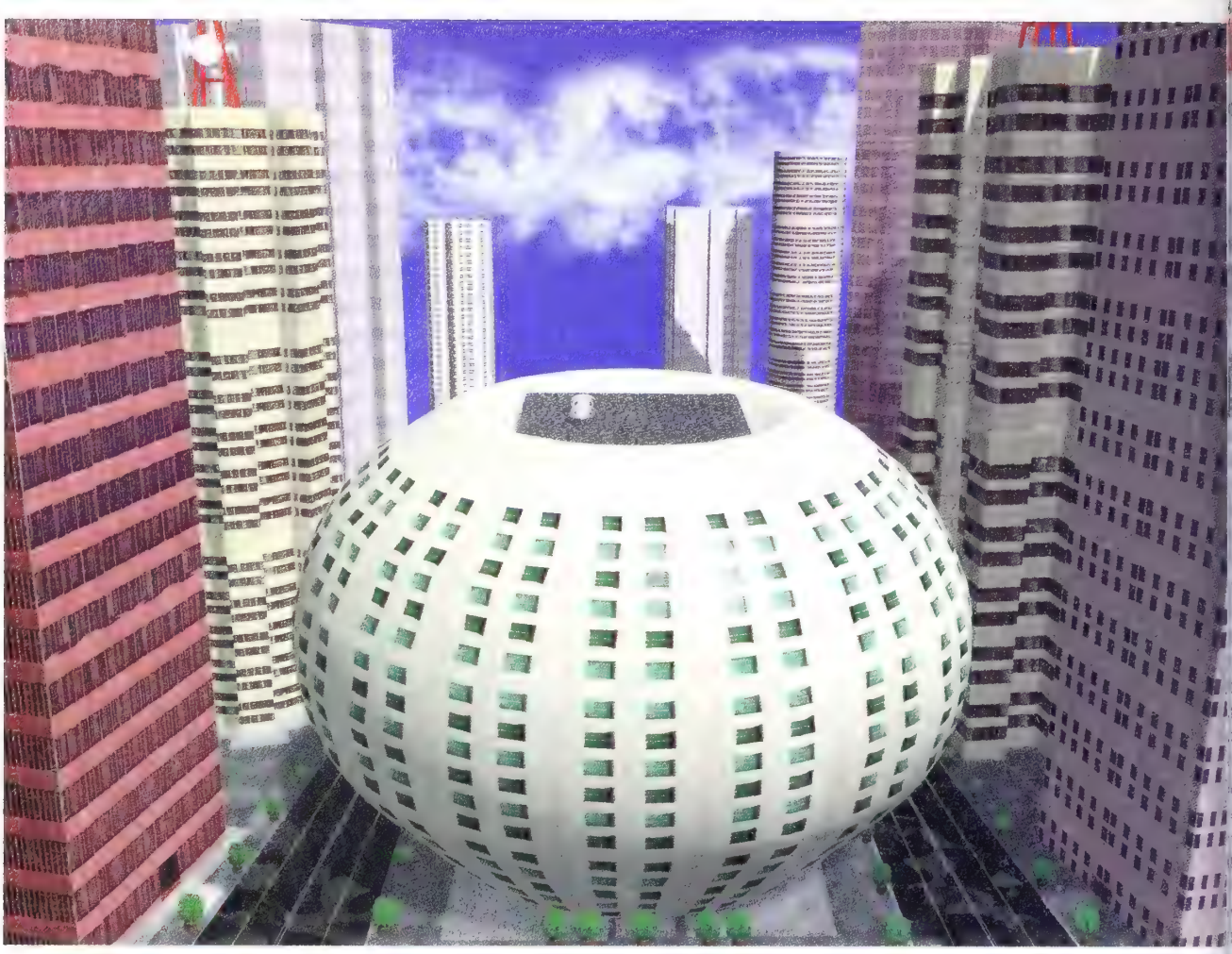


The search signals GM's new get-tough attitude toward EDS, which it plans to spin off this spring. The two companies are hammering out a new contract for how EDS will handle GM's data services after the spin-off, and sources say GM wants to slash costs. That has got to be disturbing for EDS: GM's business, $3.9 billion last year, accounts for 31% of its total revenues. GM can't get too tough because its pension fund owns 31% of EDS's stock. Still, says EDS Senior Vice-President Gary Fernandes: "GM is interested in structural cost savings wherever it can get them."

By Kathleen Kerwin and Wendy Zellner

ET CETERA . . .

- Dick Jenrette, the Equitable CEO who turned the company around, is retiring.
- Give the little guy a break: Berkshire Hathaway is issuing some low-priced shares.
- Dow Corning won a suit against insurers who failed to pay implant litigation costs.
- Phil Gramm announced that he was exiting the race for President.



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TED BY OWEN ULLMANN

CRACK IN HE CHRISTIAN COALITION

s the 1996 political season got under way, Christian Coalition Executive Director Ralph Reed made a pragmatic decision. He wouldn't rally his troops behind the ıblican Presidential candidate with the most conservative l views if it meant backing a loser. Instead, he would post es across the field to ensure an in with the eventual inee—who looked a lot like Establishment conservative Dole.

ɔunds smart, since the tax-exempt coalition is barred from ıally endorsing candidates. But Reed forgot to check with roops. The leadership may be winking in Dole's direc- but the followers aren't in the mood ɔractical politics. They're joining comtator Pat Buchanan's cultural war nst Wall Street and the Washington s. "He is another Abraham Lincoln," smitten Buchanan supporter Mitchell ɔakgian, an English teacher from Indi- a, Iowa. "He has the courage to ad- s our moral crisis without compromise."

REED: *Losing control of his flock?*

ABBLES. That's the kind of zeal leaders stifle. In the Feb. 20 Iowa caucuses, had the longest list of evangelical ac- ts' endorsements, including Iowa Chris- Coalition Chair Ione Dilley and crooner Pat Boone—but ıanan trounced the Kansas senator, 2 to 1, among self-iden- l members of the "religious right." That followed a siana caucus in which Buchanan took half of the born-again against the Christian Establishment's choice, Senator Gramm (R-Tex.), who settled for 31%. And Buchanan is ed to ride the religious wave over the next few weeks in ıaries in Arizona, South Carolina, Colorado, and Georgia, h all have potent religious machines. "What the leaders do significant, it appears," says Bay Buchanan, the candi- 's sister and campaign manager. "You win elections not a few leaders but with the activists."

ıch internal squabbling is a sign of growing pains for the 1.7 million-member coalition as it evolves from an upstart player to an enduring power broker. It has already made itself a key force behind Republican gains in recent years by registering millions of voters—and then turning them out to win targeted races from local school boards to Congress.

Moreover, social conservatives have had a major impact on the '96 Presidential campaign. Conservative Christian activists have pressured GOP White House hopefuls to move toward their agenda of abortion restrictions, gay rights curbs, and school prayer. They also helped puncture millionaire Steve Forbes's balloon in Iowa after doubting his support of a constitutional abortion ban and curbs on gays.

But success has its limits. Just ask the leaders of organized labor: Rank-and-file unionists ignored AFL-CIO endorsements of Democrats Jimmy Carter in 1980 and Walter Mondale in 1984, voting instead for Ronald Reagan. Now, the Christian Coalition is learning that its diverse membership can't be delivered as a bloc, either.

The '96 race has exposed a key fissure. There are purists who favor only staunch champions of family issues, and there are pragmatists who will settle for a candidate who is not 100% behind the social agenda—but who would pose the strongest challenge to Bill Clinton. Coalition leaders angered some purists by urging the rank and file to hedge their bets. "Ralph Reed has compromised his own convictions and those of the organization by attempting to play political power broker," says Drew R. Ivers, Buchanan's Iowa campaign chairman. "He's doing what's politically expedient rather than what's right for the country and the conservative Christian community, long term."

The lesson of '96 so far? Like other groups of voters, religious activists follow their own instincts—even if it may mean backing a losing cause.

By Richard S. Dunham in Nashua, N.H.

CAPITAL WRAPUP

HITEWATER AD NAUSEAM?

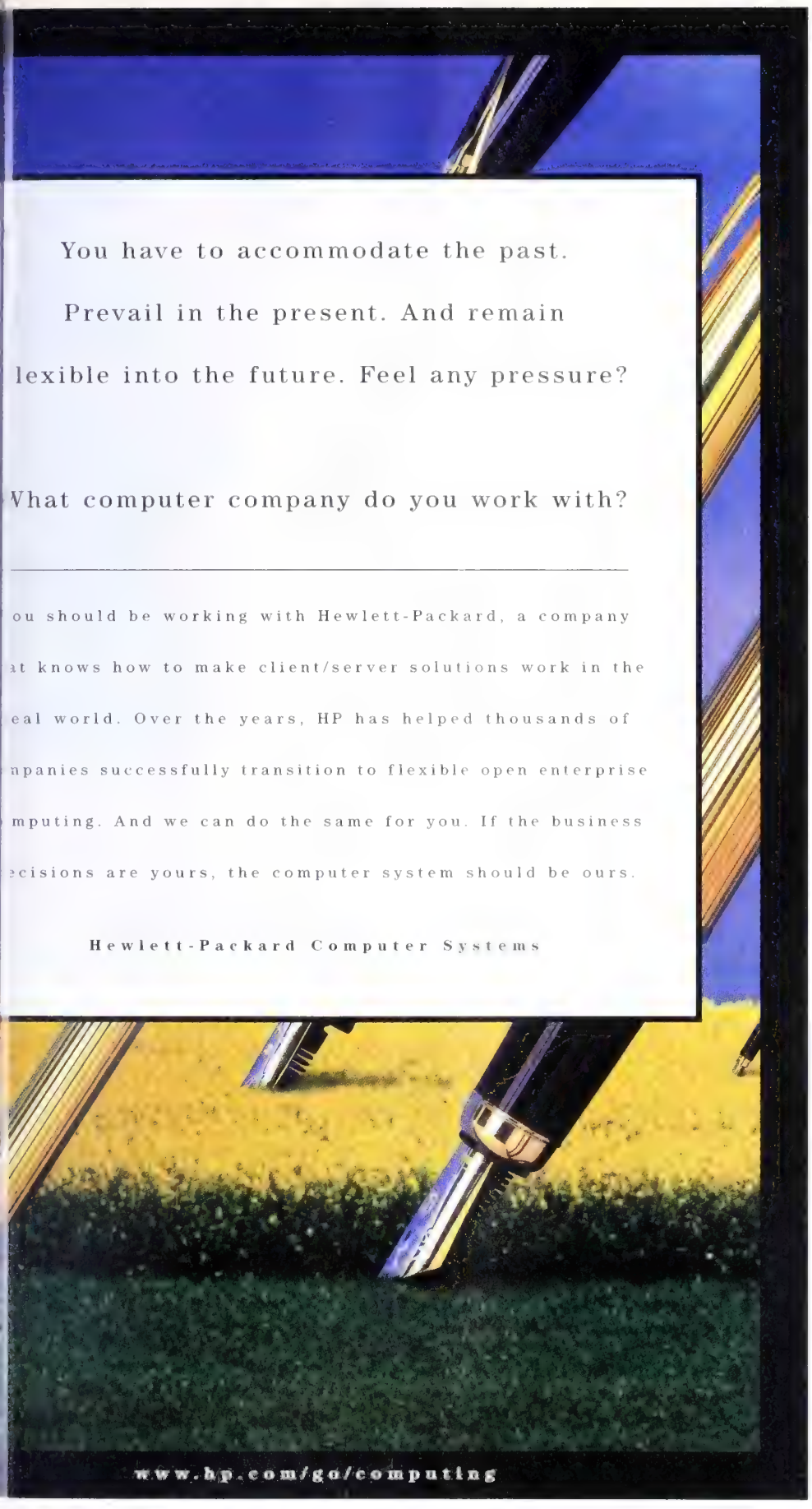
Capitol Hill Republicans can't seem delve deeply enough into Arkansas ındal. House Banking Committee airman James A. Leach (R-Iowa) is w looking into long-rumored money ındering by Arkansas banks for a ug Enforcement Agency informant spected of drug running. The nowceased informant operated out of kansas' Mena Airport in the 80s—when President Clinton was vernor. Leach may try to find out ıat Bill knew.

OZONE RIFT

▶ President Clinton, who won praise for fighting GOP efforts to weaken environmental laws, is now accused of being environmentally incorrect. The Administration wants to exempt some agribusinesses from a phase-out of methyl bromide, a chemical that harms the ozone layer. White House Chief of Staff Leon E. Panetta favors the change to win industry support in California and Florida, where the chemical is widely used. But other Clintonites fear alienating enviros.

A THRIFT IN TIME . . .

▶ Banking regulators are sounding alarms that the budget stalemate could trigger a new thrift crisis. Congress had passed a measure to make banks and thrifts shore up the nearly depleted fund that insures thrift deposits. But failure to pass a new budget has put the provision on hold. In a Feb. 13 letter to House Speaker Newt Gingrich, regulators warned that one major thrift failure could wipe out the entire $3 billion fund unless Congress acts swiftly.



HEWLETT PACKARD

ATSUSHI AND SHUKO NARA RECENTLY BOUGHT A HOME

JAPAN

WILL NERVOUS CONSUMERS JOIN THE PARTY?

Japan's recovery depends on their willingness to keep pocketbooks open

The staying power of Japan's nascent recovery will turn on consumers such as 35-year-old Atsushi Nara. Until recently, Nara and his wife, Shuko, and their two children clutched every yen. But their mood changed last year as interest rates touched historic lows and land prices settled at some 60% below their airy peak in 1991. The couple spent $470,000 on a new suburban Tokyo home and a considerable sum on furniture, and recently dropped an additional $20,000 on a new Nissan Skyline.

While such outlays hardly herald a return to the conspicuous consumption of the 1980s, Japan's consumers are showing a new willingness to open their purses (table). The extent of their spending—they account for 60% of the Japanese economy—is critical. In early February, the government cited rebounding industrial production, improving capital expenditures, and a rallying Nikkei 225 stock index as clear signs of a recovery. The economy is on track to grow 2% in 1996, but it's being driven primarily by $500 billion in pump-priming measures since 1992, improved corporate earnings, and business investment. In short, growth is tethered to the production side of the economy. For the recovery to have real legs, consumers must join the party.

Even folks such as Nara, a service representative with Hewlett-Packard Japan Ltd., still have some qualms. He's troubled by Japan's record-high jobless rate of 3.4%. "Although that's low by Western standards," he says, "we can no longer expect traditional lifetime employment in Japan."

Lifting such lingering doubts is a key preoccupation of Prime Minister Ryu

SOME BRIGHT SPOTS FOR JAPAN'S CONSUMERS

DATA: BUSINESS WEEK

PAYCHECKS

Rebounding profits
fatter wages and big
bonuses, fueling an
expected 2.5% jump
1996 consumer spe
after a four-year dro

uro Hashimoto, who is widely viewed s someone who can get the economy olling. There are reasons to think he'll acceed. True, consumer spending ipped in November and December and ersonal bankruptcies are up. Yet conmer prices have been flat, while disosable income is growing—about 1.8% the fiscal year ending in March. hat's why Barclays de Zoete Wedd esearch Ltd. economist Chris Calderood sees consumer spending reboundg 2.5% in '96 and 3.2% in '97, which ould be the highest level since '91.

Consumers are getting a big boost here it matters most—in their bank ccounts. The weakening of the yen om 80 against the greenback last April 106 on Feb. 14 played a key role. 's a boon for corporate earnings, which re expected to jump 21% this year. In rn, that takes some pressure off comanies to trim payrolls further and enres modest growth in annual bonuses, hich often represent four to five onths' pay and are a key part of most alarymen's compensation. "I believe the omestic economy has seen some righter signs," says Akira Kobayashi, 4, an executive with Eiwa Trading Co. e is expecting an increase in 1996 in is $19,000 annual bonus, and plans to emodel his home later this year.

A wave of imports—from Asian-made olor-TV sets to U.S. software and peronal computers—has helped drive down nsumer prices across a broad front. ith inflation negligible, consumers have lenty of spending power. And though eclining land prices have hurt Japanese anks and real estate speculators, the lide plus near-zero interest rates have ropelled the housing sector forward.

IG GAIN. Consider the rebound in sales f condos. The price of an average-size, 0-square-meter unit is down to 390,000—a bargain by Japanese stanards. "High-quality condos at convenient locations are now affordable," says spokesman with condo developer aikyo Inc., which expects an 18% jump sales over the next 12 months.

Consumers are also once again treaming into Japanese auto showooms looking for bargains. The auto akers logged a 5% gain in domestic ales last year, the first gain since 1990. Many buyers are driving away in economy models in the $10,000 price range. At Nissan Motor Co., which is expecting 20% sales growth in 1996, such low-priced sedans as the March and Sunny are selling well. A pickup in "consumer spending has started to brighten our recovery outlook," says Tokyo-area Nissan dealer Kozo Nakazawa.

Still, the better times don't mean a spending free-for-all. For starters, the recovery under way will be far below the average annual 7.6% bounce-back experienced in Japan's past eight postwar recessions, notes Morgan Stanley & Co. economist Mineko Sasaki-Smith. The reasons: stalled deregulation and Japan's banking mess. What's more, even the most profitable Japanese multinationals are still keeping a sharp eye on costs for fear of another bout of yen appreciation down the road.

So far, most of the job losses have fallen on members of the 50-plus crowd who have taken buyouts and on newly minted college graduates hit by hiring freezes. Should Hashimoto get serious about deregulating the economy, bigger job cuts might start showing up in such long-shielded sectors as midsize manufacturers, wholesale distributors, and mom-and-pop retailers.

If jobs start to vanish, the already frugal Japanese—who save 13% of their annual income, vs. 5% in the U.S.—could pull back in a big way. "For corporate profits to improve more, restructuring is unavoidable," says schoolteacher Keiko Yoshida, 24. She may splurge on a weekend ski trip this winter, but that's about it.

The trick for policymakers is to make sure the rebound in consumer spending isn't cut short by the cleanup of the banking mess, and that uncompetitive domestic companies are brought back to health without instigating massive job losses. It's a high-wire act. Yet if the urge to splurge can be brought back to consumers, Japan may at last be on the way to a sustained recovery.

By Brian Bremner, with Tomoko Hosoe, in Tokyo

HOUSING

g land prices and terest rates are ng the condo marhere prices have ed 23% from the e's peak in 1989

AUTOS

Ready access to cheap loans has sparked first increase in auto sales, led by economy models in the $10,000 range, since 1990

'MR. YEN' STRIKES AGAIN

Japan's economic bounce has much to do with the hasty retreat of the yen. Since last April, the Japanese currency has fallen from its 1995 high of 80 to the dollar to around 106. A good deal of the credit goes to the Ministry of Finance's Eisuke Sakakibara, deputy director general of its international finance bureau. Currency traders are calling him "Mr. Yen," for his campaign to increase Japan's capital flows overseas—a trend that undercuts the yen's strength.

CURRENCY TRADER: *A steep decline for the yen*

On Feb. 8, Mr. Yen unveiled some new tricks. He is cutting red tape on many foreign exchange deals and making it easier for offshore subsidiaries of Japanese banks to lend to foreign companies. Last August, he ended a ban on life insurance companies' making loans in foreign currencies.

In a move that could help keep the yen lower over the long term, Sakakibara will allow foreign pension fund managers nearly unlimited ability to manage Japan's $360 billion worth of company pension assets by March, 1999. The bulk of the management business has gone to Japanese trust banks, which have steered most pension money into low-yielding, but safe, Japanese government bonds as dictated by the MOF. In three years, more of that money may be invested in overseas markets; that would keep downward pressure on the yen. The changes are also coming at a time when Japanese investors are eager to borrow cheap at home, on interest rates near zero, to invest in high-yield foreign bonds and stocks.

The irony is that the MOF's triumph on the yen comes at a time when it's under broad attack for its handling of the banking mess. Nevertheless, says Deutsche Morgan Grenfell Chief Economist Edward E. Yardeni, a yen-dollar rate as high as 150 could be on the way. Not great news for Japan's competitors. But it certainly would mean an even stronger economic comeback in Japan.

By Brian Bremner in Tokyo

EUROPE

COME HOME, LITTLE STARTUPS

Europe wants its own NASDAQ to capture more IPOs

European investors have long shunned homegrown technology startups. So the Eurotech crowd crossed the Atlantic and went to the NASDAQ stock market to raise cash, much as a flock of Israeli startups has done (page 96). Now, European bourses are fighting back. Desperate to stanch the exodus of leading-edge companies, Europeans are setting up new markets where they can raise cash at home.

The latest entry: France's Nouveau Marché, which opened on Feb. 14 after a year on the drawing board. The Nouveau Marché will be followed in September by EASDAQ, a European version of NASDAQ owned by European and American investment banks and NASDAQ itself. Germany, Belgium, and Italy are also planning markets. London has one: the Alternative Investment Market (AIM), with 127 companies (table), most of them from other exchanges.

The new Euromarkets will have a tough job fighting NASDAQ to list the best Continental tech companies with global potential. "Europeans are aghast at the price we pay for small companies," says Bruce B. Bee, a global small-capitalization fund manager based in Denver. Indeed, NASDAQ issues sometimes claim valuations that are five times higher than similar listings in Europe. The Continent also lacks a research community that can analyze cutting-edge products and manufacturers. For those reasons, French software maker Business Objects turned to NASDAQ in 1994 to raise $25 million. Lernout & Hauspie, a Belgian company specializing in speech-recognition technology, raised $40 million on NASDAQ in December and has seen its stock price jump from $11 to $35.

ONLINE: *Startup Infonie's booth at a trade show in Cannes*

THE RACE TO LIST EUROPE'S SMALL COMPANIES

NOUVEAU MARCHE Paris-based small-cap stock market opened Feb. 14. Aims to list 15 to 20 companies this year, including Infonie, a local online service provider.

AIM London's Alternative Investment Market, which opened last June, is now home to 127 companies. Average daily volume: $190 million.

EASDAQ Europewide exchange modeled on NASDAQ. Owned by European and U.S. investment banks and NASDAQ. Plans to open in September.

NASDAQ The U.S. market attracted 34 European listings in 1994 and '95. Adherents argue that American investors award NASDAQ listings higher price-earnings ratios than Europeans could win at home.

DATA BUSINESS WEEK

DOWN IN FLAMES. European successe in America are luring venture- and in vestment-banking firms to the Cont nent in search of more listings. Bu some of the newcomers are also gearin up for local business. Hambrecht Quist Inc. in January joined wit France's Crédit National to form Han brecht & Quist Saint Dominique, an i vestment bank that will take companie public on the new markets in Europe

This isn't the first time Europear have tried to create a venture-capit culture. An effort in the mid-1980s wer down in flames whe a host of fund and investors los millions. But small company market ad vocates say that ver ture-fund survivors are concentratin on fewer and better-quality deal They're also cooperating with U.S. ver ture investors, who have expertise bui up over four decades in America. " took a lot of mistakes to translate th U.S. experience into doing good deals i Europe," says Helmut Schühsler, a par ner at Munich-based TVM Techno Ver ture Management.

But will Europe's new markets hav the liquidity to succeed? Europe ha only 24 IPOs last year. Schühsler est mates that EASDAQ, which is eigh months behind schedule, will need t list 100 to 200 new offerings annually t develop a critical mass. The goal may b attainable only if Europe pools its IPO

Europe's major stock exchanges ar refusing to support EASDAQ, howeve fearing it will siphon off business. Th Nouveau Marché is trying to link a the new national small-cap markets in European network to compete wit EASDAQ. Such competition could splin ter liquidity for small-cap stocks so n exchange gains enough activity to be come a contender. And the U.S. invest ment banks closing in on Europe war to post listings on both sides of the At lantic. That would create a benchmar for valuations of high-tech companies i Europe, but the U.S. might end u with the bulk of the trading. The batti for high-tech startups will be fierce. Eu ropeans insist their time has come—bu no one's handing them a victory yet.

By Gail Edmondson in Paris, wit Julia Flynn in London and Willia Glasgall in New York

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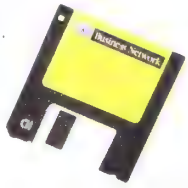

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RESUME OF A TROUBLESHOOTER

Eduardo Bours

AGE
39

BACKGROUND
His wealthy family owns Mexican agribusiness giant Bachoco

MISSION
Heads a special team that works out crippling debt problems of large Mexican companies

EXPERIENCE
Took over as CEO of bankrupt Del Monte Fresh; cleaned up balance sheet for eventual sell-off

CONNECTIONS
Well-regarded in government circles for advice on NAFTA

MEXICO

HE JUST MIGHT LOCK YOU IN UNTIL YOU DO A DEAL

Can Eduardo Bours get Mexico's banks and debtors to agree?

Eduardo Bours softpedals the toughness of his job, but the 39-year-old businessman is under enormous pressure. Bours, heir to a prosperous family poultry-raising business, has been tapped to work out deals between Mexico's banks and some of their biggest corporate debtors. "You need common sense and a cool head," says Bours, coming up for air after a long day.

Bours, who has a strong reputation as a business troubleshooter, has his work cut out for him. Talks between banks and many corporate borrowers are at a stalemate. Billions of dollars' worth of loans are going unserviced. Until the debt problem is straightened out and bank lending resumed, the prospects of a strong economic recovery will remain bleak. "One thing impeding recovery is that the relationship between the banks and bigger borrowers is very tense," says Lacey Gallagher, an analyst at Standard & Poor's in New York.

TRUSTED. Bours has the advantage of being trusted by both the banks and their customers—largely thanks to the work he did last year in rescuing Del Monte Fresh, a Mexican-owned produce company that collapsed in 1994 amid financial scandal. He also earned plaudits for his management of Bachoco, a poultry giant owned by his family, that has now been turned over to professional managers.

Bours, who doesn't receive a salary from the government, operates out of handsomely furnished offices lent by Banca Serfin, Mexico's third-largest bank. He has a team of four, chosen from the Mexican financial world and Lehman Brothers Inc. His targets are Mexico's biggest problem debtors—about 35 companies, each with debts of $100 million or more. His tactics are tough: He tries to force banks and borrowers to meet continuously until they reach an agreement. He brushes off stalling tactics with curt orders to keep talking. And he says that his good relationship with Finance Secretary Guillermo Ortiz helps step up the pressure. "The idea is that everyone concedes something," Bours says.

Bours needed only one week to restructure $120 million owed by Grupo Costamex

The strategy worked last December when Bours needed only one week to restructure $120 million owed by Grupo Costamex, a tourism company. Insiders say Bours smashed through the bank bureaucracy that was holding up the deal. He also used debt-equity swaps to restructure $440 million owed by bottle-top maker Grupo Zapata.

CONTROVERSIAL. Bours's main aim is to keep companies afloat and minimize job losses. He says he won't deal with a company unless it is viable and is willing to give up equity to creditors. Bours's biggest challenge so far has been to hammer out a plan for restructuring $2.5 billion in debt owed by Grupo Sidek, a steel and tourism conglomerate. But this project is turning controversial. Three days after Sidek announced it had reached agreement with 17 Mexican banks on $1.5 billion in debt, the company defaulted on a $20 million Eurobond. Fending off suggestions that the Mexican banks were getting favored treatment, Bours says Sidek is "not looking for debt forgiveness or reduction." He says the company wants time to raise money through asset sales. But Bours has to be careful that a Sidek pact does not hurt other companies' foreign borrowing prospects.

While most of the Mexican business community applauds Bours's efforts, the government is still taking flak for not doing enough. A major problem is that the government is trying to avoid having the taxpayers finance his deals, which limits his room to maneuver. One proposal being floated, however, involves swapping Brady bonds for corporate debt, but officials have just begun to study it.

Thousands of smaller companies below Bours's radar screen also need help with their debt. The government has come up with a $650 million rescue program for these companies. But this program likely will be used for only about 400 companies, mostly medium-size concerns employing 100 to 250 people.

Government officials say this program, Bours's mediation, and previously announced $10.8 billion in bailouts for consumers and the banks may be enough to give Mexico a push in the right direction. Just about everyone doing business in Mexico hopes so.

By Elisabeth Malkin, with Geri Smith, in Mexico City

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SADDAM MAY SNATCH YET ANOTHER VICTORY FROM CATASTROPHE

Is Saddam Hussein about to come back to haunt the West? In the five years since his humiliating 1991 defeat at the hands of the Persian Gulf war coalition, the Iraqi dictator has been kept under tight control through a trade embargo and diplomatic isolation. But at the same time, awareness has grown in the outside world that many of the 20 million Iraqis are paying a huge price for Saddam's sins. Iraq's inability to finance imports is leading to widespread malnutrition and other severe public health problems.

Now, Saddam is attempting to turn this impending human disaster into a victory for his embattled regime. In late January, Saddam indicated that he was willing to consider the one partial lifeline left to him by the U. N. Security Council: permission outlined in Resolution 986 to sell $1 billion worth of Iraqi oil every three months under strict, almost vise-like U. N. controls. The money would go into a U. N.-controlled escrow account and could only be used by Iraq for humanitarian purchases such as food and medicine. Thirty percent of the revenues would go to pay war claims, and an additional $130 to $150 million each quarter would have to go to the Kurdish areas in northern Iraq. Saddam—looking for a total end to the U. N. embargo—had always rejected such plans as a violation of Iraq's sovereignty.

SADDAM: *Will he sell oil under U.N. terms?*

GUNFIRE. But there are signs he has changed his mind. The Iraqi delegation negotiating with the U. N. in New York seems serious. And Saddam is preparing Iraqis for an oil sale. The Iraqi press has proclaimed that a deal would represent a great victory for Saddam and a humiliation for the U. S. Anticipating a shift, jubilant Iraqis hit the streets in Baghdad, firing off guns, and the battered Iraqi dinar soared against the dollar. Shipping oil would "open a psychological barrier," says Christine M. Helms, an Iraq specialist at Washington's Petroleum Finance Co. "It would give Saddam a new lease on life domestically."

That's one reason why the return of Iraq to oil markets—even in a limited form—is fraught with risks for Washington and its allies. The U. S. and key Arab states like Jordan, Kuwait, and Saudi Arabia grudgingly support the oil sales for humanitarian reasons—and as a way to bankroll the hard-pressed U. N., which would use part of the [illegible] for costly weapons-monitoring operations inside Iraq. Also, a weakened Iraq [illegible] sell some oil is preferable to the [illegible] Bosnia-style breakdown of a country that has long been a buffer against Iran. It may be hard to draw the line at limited sales. The French and the Russians, who have lon[illegible] been trying to bring Iraq back into the market, may take an[illegible] deal as a cue to push for more. At the same time, it will b[illegible] hard to cut off the flow if Saddam misbehaves. Turkey, whic[illegible] will receive fat transit fees from Iraqi shipments, will resi[illegible] any cutoff. So will Egypt and other key developing countrie[illegible] that are disturbed about the deteriorating conditions in Ira[illegible]

Even limited sales will whack the oil market. John L[illegible] Lichtblau, chairman of the Petroleu[illegible] Research Foundation in New Yor[illegible] reasons that the impact of 700,000 t[illegible] 800,000 barrels a day of Iraqi oil sud[illegible] denly coming to market would cause [illegible] "significant" decline in prices of $2 t[illegible] $3 a barrel. That would be unwelcom[illegible] news for Saudi Arabia, which is st[illegible] struggling with $100 billion in dome[illegible] tic debt. But the real fear for th[illegible] Saudis and other gulf states is tha[illegible] Iraq will eventually find a way of ge[illegible] ting its production back to its prewa[illegible] 3 million-plus barrels per day.

More disturbing for the U. S., Ru[illegible] sia is emerging as a wild card in th[illegible] Iraqi game. Signs point to Russia pu[illegible] suing a much more assertive polic[illegible] in the Middle East under new Fo[illegible] eign Minister Yevgeny Primakov[illegible] one of the former Soviet Union's ke[illegible] Mideast experts. "We've come to th[illegible] conclusion that Iraq's policies and co[illegible] duct comply with the demands of th[illegible] U. N. Security Council resolution," says Viktor A. Kremenyu[illegible] deputy director of Russia's U. S. A.-Canada Institute. "W[illegible] think it's high time to end the embargo."

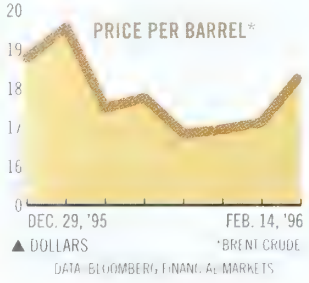
The motive is partly economic: Russia wants to see repay[illegible] ment of Iraqi debts of $7 billion and give a boost to its arm[illegible] and energy industries. Russian oil giant Lukoil, eager to pu[illegible] down stakes in the Persian Gulf, is behind a recent $10 billio[illegible] agreement to rebuild Iraq's damaged oil industry. France's T[illegible] tal and Elf Aquitaine also have Iraqi deals lined up.

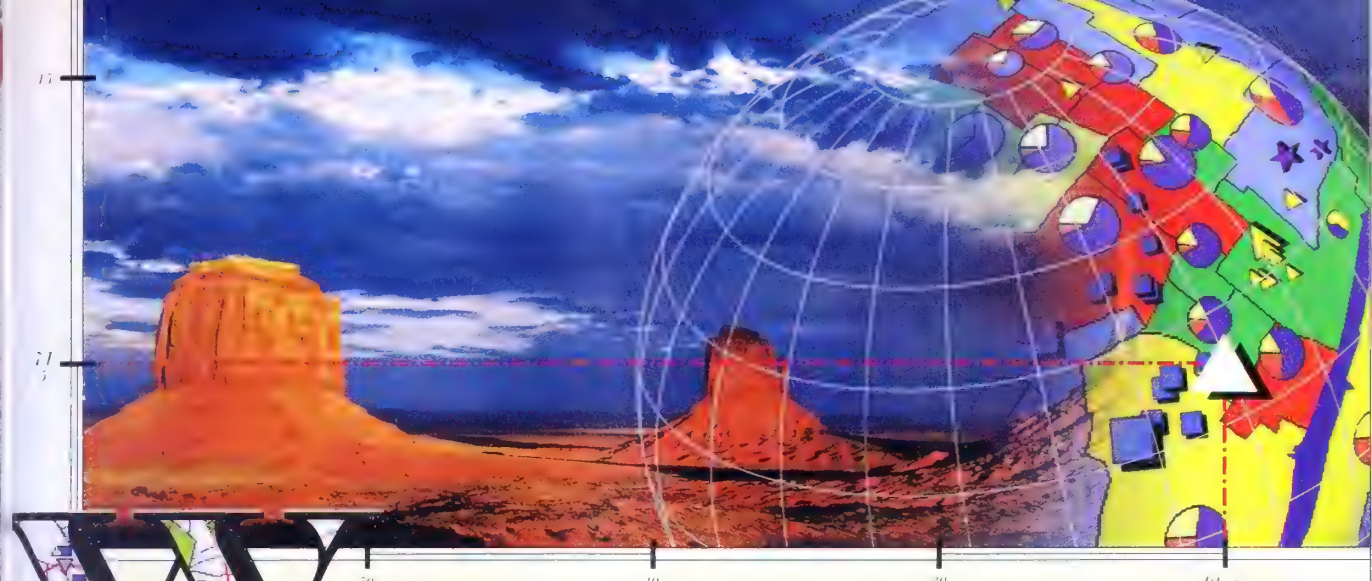
But there is a political component, as we[illegible] The view in Moscow is that Russia has giv[illegible] en up too much of its global clout, especial[illegible] in the Middle East, where it once rivaled th[illegible] U. S. Russia is already letting the We[illegible] know that a projected expansion of NAT[illegible] into eastern Europe could result in Russia[illegible] unilaterally lifting the Iraq embargo.

So, battered as he is, Saddam is still [illegible] thorn in America's side. Few envisioned suc[illegible] an outcome five years ago, when the gu[illegible] war ended with the allies deciding not to g[illegible] on to Baghdad.

By John Rossant in Rome, with Patrici[illegible] Kranz in Moscow and bureau reports

THE IRAQ EFFECT: OIL MARKET JITTERS





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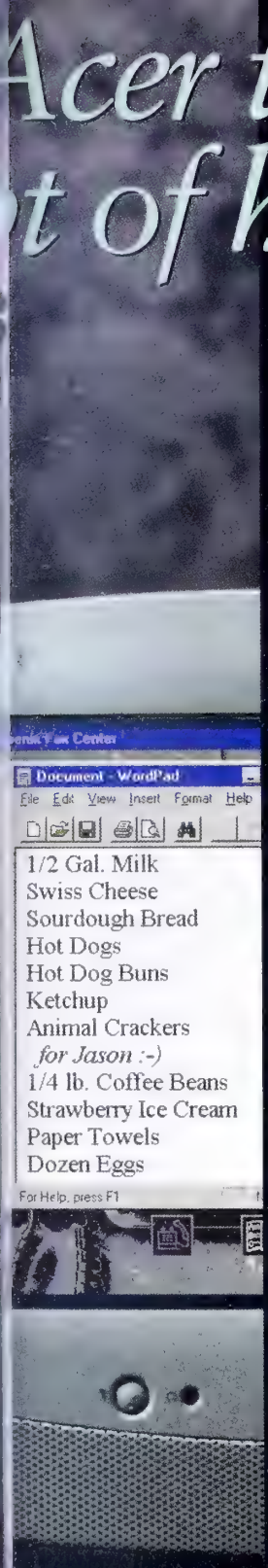

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STRATEGIES

REEBOK IS TRIPPING OVER ITS OWN LACES

In the teen market, it keeps stumbling after Nike

For Reebok Chairman Paul Fireman, stealing Jack Steinweiss from Fila Corp. last March was the high point of an otherwise lousy year. As creator of Fila's Grant Hill shoe—a best-seller endorsed by the Detroit Pistons' star—Steinweiss was hot. With sneakers from Reebok International Ltd. losing favor among teens, Fireman counted on Steinweiss to recapture part of the youth market dominated by Nike Inc.

But by yearend, Steinweiss had become one more in a long list of problems facing the Stoughton, Mass., company. After just nine months, the star designer returned to Fila. Steinweiss says he left because he had little influence over new products—a complaint that goes to the heart of what ails Reebok. With development hobbled by massive management turnover, high-level infighting, and strategic blunders, Reebok has stumbled repeatedly.

The result is a sneaker company's nightmare. Teenage boys account for a 20% slice of the $6.8 billion U.S. athletic-shoe market. Rival Nike's popularity among teens helped propel its share of the overall market from 31% to 37% in 1995, while Reebok slid two points, to 20%. As a result, Reebok's sales rose just 6%, to $3.5 billion in 1995, while income sank 35%, to $165 million; this year, analysts expect Reebok's sales to grow an anemic 4%, to $3.6 billion. Meanwhile, analysts expect Nike's sales for the fiscal year ending in May to jump 24%, to $5.9 billion, while earnings should rise 57%, to $508 million.

Trailing behind Nike is nothing new to Reebok. But the current problems are its toughest yet, and Wall Street is losing faith in Fireman, who gained control of Reebok in 1984. Last summer, big shareholders called for his ouster. After he rebuffed his critics, many sold out. Since April, Reebok shares have sunk 25%, to 28. "Fireman is a classic case of a guy who starts a business well but can't run things at a later stage," says shareholder activist Nell Minnow of Lens Inc.

Fireman, who holds a 14.5% stake, declines to comment. But he seems to have backing from a board dominated by local executives. "Reebok's record over the last 10 years has been phenomenal," says director Geoffrey Nunes, general counsel to chemical purification outfit Millipore Corp. "There's no reason to think Paul is not as capable today."

Reebok's current ills began in 1993, when Fireman backed a poorly conceived attempt to take on Nike's dominance of professional sports and the men's performance sneaker market. Until then, Reebok's popular aerobics shoes and a reputation for comfort allowed it to reign over women's sneakers. But slowing growth convinced Fireman that Reebok needed stronger shoes for men and boys, and he tapped Robert Muller, the former owner of rival shoemaker Pony Sports & Leisure, to help. To its credit, Reebok has since built a high profile with athletes. Among its star endorsers are Orlando Magic center Shaquille O'Neal and Dallas Cowboys running back Emmitt Smith. Reebok shoes will also be worn by 3,000 athletes at the Summer Olympics. And it has developed a big name in soccer shoes abroad, giving Reebok an international business that rivals Nike's.

SHAQ ATTACK: *The O'Neal-endorsed Shaqnosis is Reebok's flagship shoe*

LIGHTNING ROD. But the gains pale in comparison to problems created by the shift. Costs soared: Sales, general, and administrative expenses rose to 32.7% of revenues in last year's second quarter, up from 24.4% in 1991. And former and current executives say the push to create shoes for pro athletes generated huge internal strife. Says one: "In military terms, we took our objective but left our soldiers dying on the battlefield."

Inside Reebok, Muller became a lightning rod for controversy. As Reebok's co-president, the strong-willed executive ruled over product development and design. He ordered dozens of high-performance sneakers at a rapid-fire pace. But one group of managers, led by fitness division head Edward Lussier, argued that Muller wasn't producing innovative designs but simply copying Nike. After Lussier left for Adidas in 1993, the battle continued. Last year, 50% of Reebok's design staff left, along with other marketing and product development managers.

At the same time, Muller

Some more bars for Fireman his second

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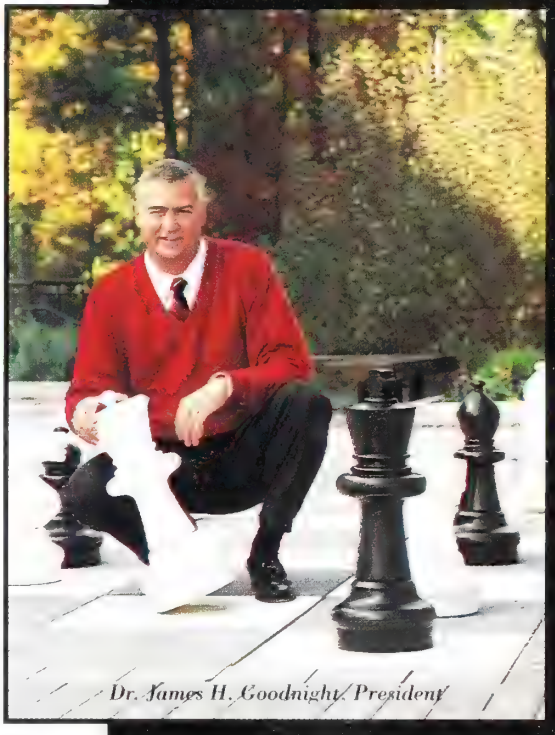

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er took Reebok out of the top of the market, where prices run from $100 to $130. He argued that Reebok could make high-quality sneakers to sell for less than $90. But the move backfired badly when the market for top-dollar sneakers surged in 1994. Reebok had no flashy high-tech models, while Nike cleaned up with its Visible Air shoes, which sport a see-through air bubble under the sole.

The upshot: Even as Reebok spent millions signing athletes to draw teenagers, it had no strong products to sell them. Instead, the effort to quickly churn out dozens of different shoes for many sports resulted in average-looking shoes that excited no one. "Reebok completely missed the market," says Ken Crystal, owner of Crystal's of Boston, a shoe store catering to urban teens.

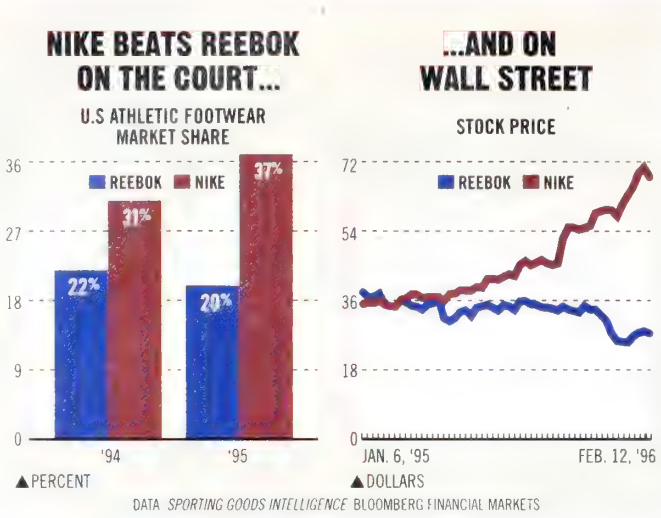
Meanwhile, former managers say Fireman was barely aware of the infighting. "He was in and out," says a former top aide. When he was around, they complain he focused on a pet project, the InstaPump shoe. But the shoe, which needs a hand-held pump to inflate, hasn't caught on, further draining resources.

With problems mounting, John H. Duerden, Reebok's marketing head and co-president, pushed Fireman to name him CEO last spring. When Fireman refused, Duerden quit. Three months later, Muller also left under pressure.

The turmoil helped sour Reebok's relations with Shaquille O'Neal. He was so upset with the shoes Reebok made for him—and the ineffective promotional job it did—that he shopped for a new contract last summer. Reebok Marketing Vice President Peter Moore admits that relations with Shaq are "like the Cold War." O'Neal's agent, Leonard Armata, says they're now "working fastidiously" to reach a new accord.

MIXED REVIEWS. But the Cold War may be Reebok's easiest problem to solve. Shaq is far happier with this year's new psychedelic Shaq-nosis model. Although shareholders called for a strong outside CEO last summer, Fireman named longtime confidante Robert Meers—who ran the Reebok Brand Div. before Duerden and Muller—to the job in November. Fireman also put himself in charge of product design.

The results of Fireman's work won't show until 1997. In the meantime, retailers have given mixed reviews to Reebok's 1996 shoes. To gain a march



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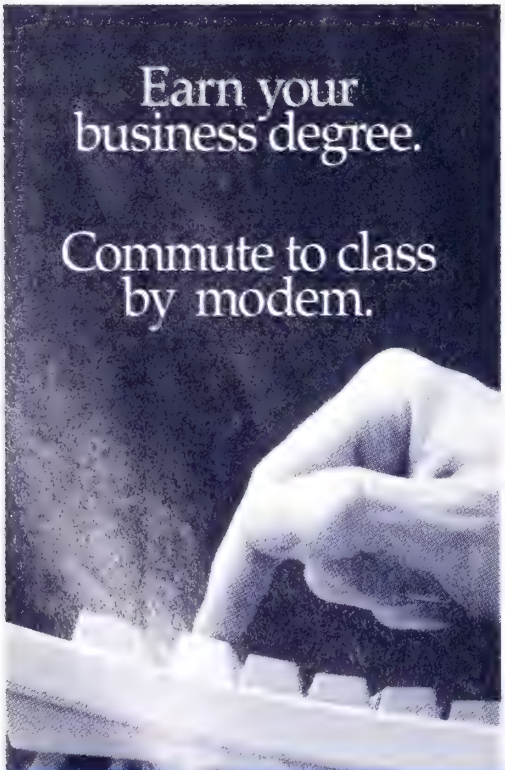

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on Nike, Reebok plans to launch its new Vishex shoe this fall. Featuring a honeycomb-celled air bladder, it's the cornerstone of Reebok's return to the high-price, high-tech shoe category. But Charles Gore, vice-president for merchandising at Herman's World of Sporting Goods, worries that teens might see the me-too air approach as a gimmick. Even Meers concedes that Reebok is unlikely to gain significant share this year.

"FLAGELLATION." In the meantime, Fireman has some unorthodox methods for revitalizing the company. A follower of EST, Fireman last year hired a consultant with techniques rooted in the controversial therapy. The purpose: to provide three-day "leadership training" sessions to 500 Reebok managers. One exercise: writing to the person you hate the most in the company and reading it publicly. Says one executive: "There's crying and anger, and you commit to a team effort."

Not everyone likes the sessions; one former executive dismisses them as self-flagellation. "You can't tell the chairman it's garbage," he says. "The rest of the company had to grin and bear it." Still, several managers say once tense communications have improved. "It sounds like Business 101, but we've gotten people to talk the same language," says Dan Dobrzynski, Reebok's vice-president for advanced products and processes.

Other changes are more traditional. Late last year, Meers stripped Reebok's marketers of control over design. Designers and manufacturing experts now work together on product-development teams—and Reebok marketers simply sell what they're given. A plan to cu $75 million in costs was completed las September. Reebok also recently took $49 million charge to sell its underper forming Avia women's shoe line. Nev ads meant to clarify Reebok's muddy image have also been launched.

So far, outsiders remain unimpressed "They're playing catch-up," says Smit Barney Inc. footwear analyst Faye Lan des. And Glenn Greenberg, managing director of Chieftain Capital Manage ment, which sold 4.5 million Reebok shares in November, says he has com pletely lost confidence. "Reebok is like fish flopping around on a deck," he says With reviews like that, Fireman's tough times look far from over.

By Geoffrey Smith in Stoughton, Mass

FILA'S FULL-COURT PRESS TO SNARE SUBURBIA

Strolling along New York's Broadway, Sadiki Nokwere steps into a shop to buy a sporty-looking Fila shirt. The 30-year-old musician had already purchased two pairs of Fila pants elsewhere that day. "I like the design and the feel," he says. "I buy it to be unique."

If Nokwere really wants to be unique, he may have to find another brand. Last year, Fila rocketed from seventh to third place in the U.S. athletic-shoe market. Its clothes are huge in the inner city. And with new apparel and shoe lines on the way, Fila Holding—based in Biella, Italy—now wants to clothe older suburbanites, too. "Only companies that are able to break out of their urban niche can survive," says 61-year-old Enrico Frachey, Fila's chief executive.

It's a risky bet: Despite its history as a maker of preppy tennis togs and skiwear, the 70-year-old Fila's resurgence stems from the appeal of its boldly designed sneakers and casual wear to city teens. Fila's comeback began when Frachey, its former No. 2, returned to the money-losing company as CEO in 1987. By 1993, after Frachey had set up U.S.-based management, hired hip designers, and begun signing stars, Fila went public. But it wasn't until last March that Fila struck gold with its Grant Hill shoe, named for the 1995 NBA rookie of the year. The basketball shoe brought in roughly 20% of U.S. sales, catapulting Fila past such rivals as Adidas.

KING OF THE HILL: *Fila's Grant Hill shoe is a smash with city teens*

U.S. sales have jumped from $84 million in 1991 to roughly $500 million last year—57% of Fila's estimated total sales of $879 million. Analysts expect 1995 profits to rise 40%, to $60 million. That has sent Fila's American depositary receipts soaring 148% in the past year, to around 50. "Fila is the strongest up-and-coming brand in the industry," says analyst Kevin Tempestini of Salomon Brothers International in London.

To keep up momentum, Fila's new U.S. footwear head, Robert Liewald—the ex-corporate merchandiser for Foot Locker and Woolworth Corp.'s other athletic-shoe divisions—is putting on a full-court press: A new Grant Hill shoe came out in November, and a summer campaign will tie his Olympic appearance to another shoe. Other endorsers include star rookie Jerry Stackhouse of the Philadelphia 76ers—who has a five-year, $15 million deal—Randy Stoklos, of beach volleyball fame, and marathoner German Silva.

BOOMER BOUND? But the biggest challenge will be broadening beyond Fila's niche. Frachey knows that its faddish popularity could quickly disappear. So he wants to boost non-shoe sales in the U.S., now roughly 23% of revenues here. With a men's clothing line, Fila Sport, skiwear, and outdoor gear, Frachey is aiming for an older, wealthier market.

Will Fila's hip, street-smart appeal catch on among aging suburban baby-boomers? "The Fila label is so heavily associated with the inner city that suburban types might not relate to it," says Robert E. Carr, editor of the New York-based *Inside Sporting Goods* newsletter. Indeed, the risk of being all things to all people is that neither Sadiki Nokwere nor his suburban counterparts may feel unique with Fila.

By Silvia Sansoni in Biella, Italy, and Lori Bongiorno in New York

Clearly, the people at Dodge are having way too much fun.

Intrepid ES features: • cab-forward space and stability • 3.5L, 24-valve V-6 engine • speed control • power windows and door locks • 16-inch touring tires • fog lamps • power heated outside mirrors • driver and front passenger airbags • air conditioning • AM/FM cassette and center console with storage • available AutoStick® System transmissio • more trunk and passenger room and better resale value than Taurus, Lumina or Camry.† Intrepid starts at $18,99 Intrepid ES shown, $23,010.

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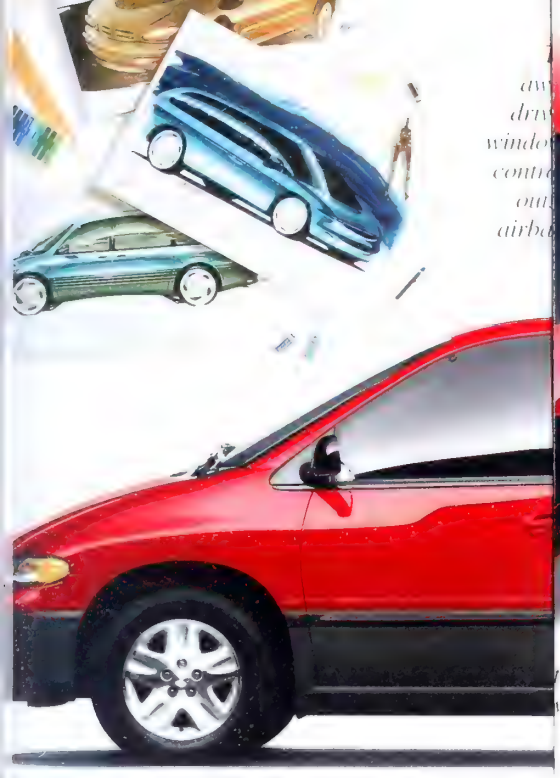
Stratus starts at $14,770.
ES shown, $16,795.



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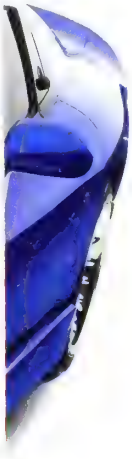

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NEWSPAPERS

RUNNING HARD, BUT STAYING IN PLACE

Knight-Ridder is still reliant on slow-growth newspapers

Knight-Ridder Chief Executive P. Anthony Ridder fancies himself a man of action and more important, speed. His friends and colleagues say he drives fast, skis fast, and even golfs fast. But the activity that Ridder is pursuing the most frenetically these days is the rejiggering of his $2.8 billion newspaper and information company.

Ridder has held the top job at the company founded by his great-grandfather for only 11 months. In that short time, he has engineered a flurry of cost-cutting measures and asset sales and has nearly completed a transformation of the company back to its newspaper roots. But while the cost-cutting pleases investors, Ridder has yet to come up with an answer to the knotty problem the company has long faced: how to find growth in the mature newspaper business.

NO FIT. At cost-cutting, at least, Ridder has proved to be a pro. Last March, he sold the *Journal of Commerce* for $115 million, arguing that its focus on international trade and transportation didn't fit with the company's core regional-newspaper business. In August, he pulled the plug on a design lab that had been developing a futuristic flat-panel news "tablet" that would have delivered newspaper content to consumers electronically. Last month, Ridder put Knight-Ridder Financial on the block after it failed to make headway against rivals Bloomberg, Dow Jones Telerate, and Reuters. And Ridder's tough stance in the seven-month-old strike at Detroit Newspapers Inc., which publishes Knight-Ridder's *Detroit Free Press* and Gannett Co.'s *The Detroit News*, proves he is willing to stomach substantial losses now in exchange for lower labor costs in the future.

The moves have drawn plaudits from analysts and shareholders. Knight-Ridder had been experiencing some "stagnation and lack of focus. Ridder brings vitality and a sense of urgency," says Henry Berghoef of Harris Associates, which holds more than 5% of the company's stock. Other shareholders are happy, too. In the past six months, the company's long-lackluster stock rose 18%, to about 67.

CEO RIDDER: *He has cut costs but found little new revenue*

After all the cost-cutting, though, Knight-Ridder still finds itself in much the same position it held in the 1980s, when it embarked on a string of ventures aimed at reducing reliance on slow-growth newspapers. Most of those ventures have since been closed or sold (table). The company still derives more than 85% of its revenues from 31 dailies in such cities as Philadelphia, San Jose, Calif., and its home base of Miami. And its operating margins on those newspapers are dispiritingly slim, at 12.5%, says analyst John Morton, while the industry averages 14%. Margins at rivals Tribune Co. and Gannett routinely hit 20% or more.

BRISTLING. Ridder needs to find new and better sources of revenue, and that's not easy in the newspaper business. Some wonder if Ridder, 55, is up to the task. "There are no growth prospects and no model in his head as to where [growth] is going to come from," says one former executive. Ridder rejects that notion. "I bristle when people say we're only cost-cutting, because we're trying to build revenue," says Ridder, who has worked for the company his entire career.

Ridder's most aggressive move on that score was to spend $360 million in June for four small newspapers in California's fast-growing Contra Costa County. He sees the acquisitions as a pricey but strategic complement to the

KNIGHT-RIDDER'S TRIALS AND ERRORS

The company has aggressively launched new ventures over the past decade or so, only to pull out when costs or risks got too high

VIEWTRON Launched in 1983, the videotext service was closed in 1986, after the company spent $50 million.

TV STATIONS After about a decade in the TV business, Knight-Ridder sold all eight VHF network affiliates in 1989 to finance yet another news-retrieval service.

INFORMATION DESIGN LAB Created in 1992, this R&D unit experimented with electronic newspapers, including a flat-panel display for delivery of content via phone lines or wireless. Shuttered in '95.

KNIGHT-RIDDER FINANCIAL Formed in 1985, this provider of real-time and archival financial data never made headway against rivals. Put up for sale in January.

DATA: COMPANY REPORTS

company's neighboring San Jose paper. But the purchase only heightens the company's reliance on its newspaper business.

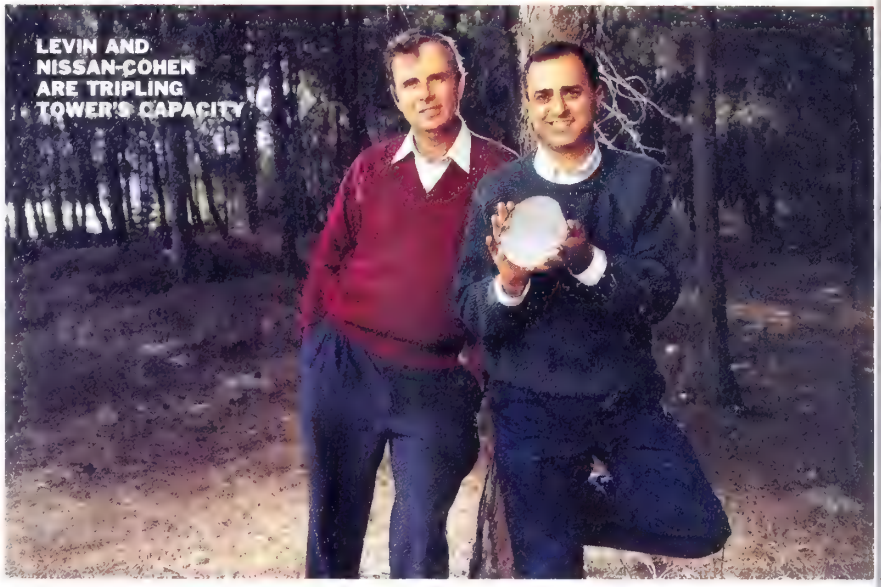
Otherwise, Ridder is trying to squeeze more from what he has. He's demanding better operating margins from his dailies, particularly *The Philadelphia Inquirer* and *The Miami Herald*, which have cut employees and publication of some zoned editions. And he raised the stakes for all Knight-Ridder publishers last year by tying a substantial portion of their bonuses to getting 3% of new revenue from new ventures such as special sections, guides, and audio-text services. That effort generated more than $50 million in new revenue last year, which constituted half the companywide revenue gain of 3.9%, to $2.8 billion.

As modest as that initiative sounds, it's the clear winner among Ridder's grab bag of growth schemes. Other ventures tried over the past few years have met with little or modest success. For example, most of Knight-Ridder's newspapers have tried capitalizing on their expensive distribution systems by delivering magazines, but logistical and advertising problems have largely crippled the plan. Other efforts to offer a package of options to advertisers beyond the traditional newspaper, such as sponsoring women's conferences and holiday shows, issuing niche publications, and dabbling in database marketing, haven't yet amounted to much.

BACK ONLINE. Ridder hints that the company may soon reenter the television business, perhaps in a joint venture with a national broadcaster that will build on the company's newspaper markets and provide new opportunities for revenue. Knight-Ridder got out of television in 1989, when it sold its eight-station group to help finance the $353 million acquisition of Dialog, an information retrieval service used mostly by librarians.

Ridder is also putting Knight-Ridder back online. In the 1980s, its Viewtron online service was a pioneer on the Information Superhighway until Knight-Ridder scuttled the effort in 1986. Now, Ridder plans to have all of Knight-Ridder's papers online, via America Online or the Internet, by early 1997. But this time around, Knight-Ridder will be producing only the content and won't be making another costly investment in creating an electronic distribution network. Until any substantial new revenues from the electronic age take hold, Knight-Ridder remains squarely in the same old newspaper business. And Ridder finds himself running faster just to keep up.

By Gail DeGeorge in Miami



LEVIN AND NISSAN-COHEN ARE TRIPLING TOWER'S CAPACITY

SEMICONDUCTORS

A CHIP UPSTART IN GALILEE

No freelance chipmaker outside Asia rivals Tower in size

Bankers laughed in 1992, when Yoav Nissan-Cohen and Rafael M. Levin asked for money to buy a National Semiconductor Corp. chip plant in Migdal Ha'emek, Israel, where they worked. They wanted to convert the plant, which National had put up for sale, into a "foundry" that would make chips under contract for other companies.

The bankers' derision was understandable. Contract manufacturing of chips wasn't considered a healthy business in the early 1990s. Taiwan Semiconductor Manufacturing Co., today the world's largest foundry, hadn't yet proved that such chip factories can be highly profitable.

WELL-TIMED ENTRY. Happily for the entrepreneurs, George Morgenstern didn't laugh. The head of Data Systems & Software Inc. in Mahwah, N.J., saw a steal. Because National was restructuring, it was willing to part with an 80% stake in the plant for just $20 million, mostly assumption of debt. Morgenstern coughed up a $4 million downpayment, then sold 40% of his stake for $8 million to Israel Corp., a holding company headed by billionaire Shaul Eisenberg.

It turned out to be a huge bargain. A worldwide explosion in semiconductor markets is creating an insatiable demand for foundry-made chips. A case in point: Taiwan Semiconductor's revenues soared 49% in 1995, to $1.2 billion, and its profit margins were 55%—even better than those of Intel Corp.

Nissan-Cohen and Levin are hardly in that league. But the company of which they are co-CEOs, Tower Semiconductor Ltd., is the biggest foundry outside East Asia. It has posted sales growth of 60% a year, with profits more than doubling in each of the past two years. Earnings topped $20 million in 1995, on sales of $99.6 million. Morgenstern's $4 million gamble is now worth $80 million. These are heady times for Nissan-Cohen and Levin, both of whom have doctorates in physics and spent several years in the U.S.—Nissan-Cohen at General Electric Co.'s research center and Levin at AT&T Bell Laboratories. Says Nissan-Cohen: "Our entry couldn't have been timed better."

National is still the plant's leading customer. "All of the products we were

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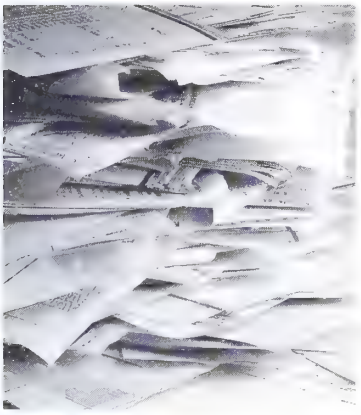

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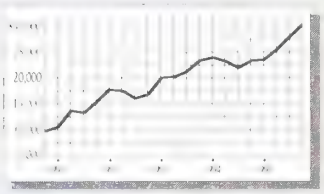
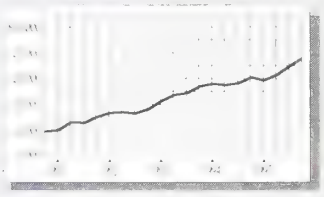
INVESCO DYNAMICS



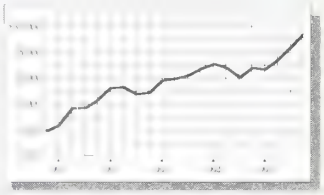
Value of investment: $30,583
Average annual returns (as of 9/30/95):
1 year +29.97% 5 year +25.05%
10 year +15.69%

STRONG OPPORTUNITY



Value of investment: $24,180
Average annual returns (as of 9/30/95):
1 year +18.57% 5 year +19.31%
Since inception (12/31/85) +18.32%

FOUNDERS SPECIAL



Value of investment: $28,702
Average annual returns (as of 9/30/95):
1 year +29.29% 5 year +23.48%
10 year +17.45%

MORNINGSTAR *Data provided by Morningstar, Inc. as of 9/30/95. These and over 350 funds are available through Schwab's Mutual Fund OneSource.*

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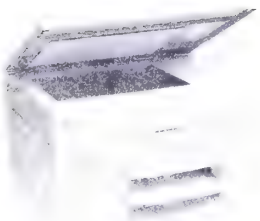
It prints. **It copies.**

(It does not, unfortunately, monitor taste.)



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Look at the vivid color. Look at the flawless reproduction. Don't look at the hat. What's important is that the new CopyJet gives you the quality you'd expect from an HP color printer, and it has the full functionality of a color copier. Besides the departmental convenience, the CopyJet is easy to operate and uses plain paper. If the whole department needs color printing and copying, there's the network-ready HP CopyJet M, for $3199. That's just a fraction of the money you won't have to spend for color copies. Which will make you look good, no matter what you're wearing.

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HEWLETT PACKARD

producing there are still being produced there today—but in greater volume," says George M. Scalise, National's executive vice-president. Other customers include Motorola, Hewlett-Packard, and Chip Express, an Israeli startup that has developed a system for producing chips in as little as one day in volumes as small as one chip (box).

DUTY-FREE ADVANTAGE. Each of Tower's customers prescribes slightly different chipmaking processes that are tuned to its chip designs. Tower engineers work with the customers to make sure process matches product. Nissan-Cohen argues that attention to such details distinguishes Tower from its larger competitors. But some analysts say Tower is simply benefiting from the overall growth of the sector. "They're not doing something special," says John Chen, an analyst at VLSI Research Inc. in San Jose, Calif. "This is just a good time to be in the foundry business."

To prepare for more growth, Tower is adding a third floor to its building, nestled in the Galilee hills near Nazareth, and converting ground-floor offices to manufacturing. The $240 million project will triple capacity from three years ago. Later, Tower wants to build a $900 million chip plant, or fab, that would triple production again.

Levin and Nissan-Cohen can't hope to match the expansion plans of their East Asian competitors. Taiwan Semiconductor began building a pair of billion-dollar fabs, its fourth and fifth, even before fab No. 3 started production last fall. Similar expansions are under way at Singapore's Chartered Semiconductor Manufacturing and Taiwan's United Microelectronics. Instead, the co-CEOs are focusing on locking in key customers. Says Levin: "We stress strategic alliances that force us to adjust to the customers' needs"—so customers won't see much gain from shifting to a rival to get a lower price.

Being in Israel gives this toddler of a foundry an edge on its giant Asian competitors: Tower can export chips duty-free to the U.S. and Europe—and it has barely begun to tap demand in Europe. The onetime white elephant is shaping up as one profitable pachyderm.

By Neal Sandler in Jerusalem

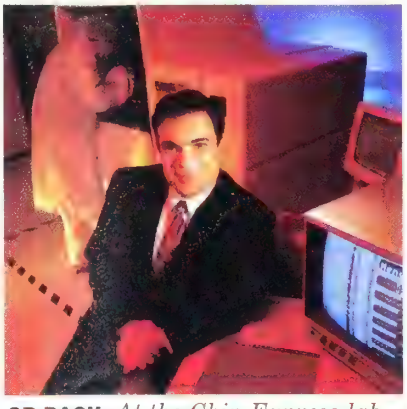
A SHORT-ORDER CHIP CHEF

For defense contractors and other companies that buy chips in small volumes—or for product-development teams on a deadline—Chip Express Corp. can be a lifesaver. The Santa Clara (Calif.) company can produce chips one at a time, although it prefers to make at least 10 copies. "We're bringing a machine-shop approach to making chips," says President Zvi Or-Bach.

The cost? About $8,000 for the first two chips, with discounts for longer runs. But for a cash-strapped startup, Or-Bach will do the first chip free.

Chip Express is also fast. For National Semiconductor Corp., it once came through with a handful of chips in two days, vs. four weeks for National's own chipmaking operation.

CROSSBAR NETWORK. The secret is a miniature chip plant not much bigger than a desk—and special silicon wafers with windows, from Tower Semiconductor Ltd. The wafers have metal circuit lines running one way on the surface, while tiny windows peer down on more lines underneath, at right angles. So each chip-to-be is a massive crossbar network. To turn this grid into a circuit, a special laser selectively burns through metal lines on both layers—often making several million cuts, at 20,000 per second.



OR-BACH: *At the Chip Express lab*

Privately owned Chip Express says 1995 sales were $18 million, almost double the year before. Its popularity is understandable. "Being first to market can spell the difference between healthy margins and mediocre profits," says Or-Bach. That could make $8,000 for the first two chips look like a steal.

By Otis Port in New York

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Call now or contact us at http://www.hp.com/info/1133 and we will send you print samples demonstrating the incredible color reproduction of the HP CopyJet. We will also be glad to include a detailed product brief explaining our inkjet technology with precision digital color imaging. Find out about the HP CopyJet and start saving money on color printing and copying today. A year from now you'll be happy you did.

HEWLETT PACKARD

Otis Carrier Pratt & Whitney Sikorsk

Breaking new ground is most critical to companies that manufacture:

- jet engines
- air conditioning systems
- helicopters
- automotive systems
- elevators
- aerospace control systems

---------- (Note: pick six)

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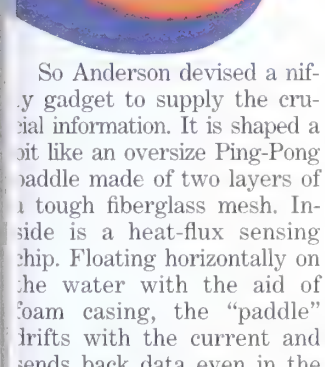
WHAT'S NEW AT THE SCIENCE BAZAAR

Highlights from the most eclectic research meeting of the year

THE ANNUAL MEETING OF THE AMERICAN ASSOCIATION FOR the Advancement of Science in Baltimore last week brought together leaders from all walks of research. Discussions ranged from the behavior of atoms to exotic applications for "artificial life." John Carey, Otis Port, and Paul Raeburn report:

A WAVE-TOP TOOL TO TRACK HURRICANES

THE FORECASTING OF TROPICAL storms is still an inexact science, in part because meteorologists don't usually have the luxury of cruising the seas to take measurements. One key parameter, for example, is how much heat is transferred from the ocean to the atmosphere. "These storms are driven by the heat flux from the oceans," explains John R. Anderson of the University of Wisconsin.



So Anderson devised a nifty gadget to supply the crucial information. It is shaped a bit like an oversize Ping-Pong paddle made of two layers of a tough fiberglass mesh. Inside is a heat-flux sensing chip. Floating horizontally on the water with the aid of foam casing, the "paddle" drifts with the current and sends back data even in the roughest weather.

One of Anderson's first ocean experiments showed how valuable that data can be. During tropical storm Alison, the measured heat transfer was only one-tenth what meteorologists had expected, and the storm failed to follow its predicted course of development. Anderson is now fortifying the devices to protect them from ospreys and other birds, which clawed the foam and fiberglass mesh. When he puts a fleet of them in the Gulf Stream this year, the result may be significantly improved forecasts of hurricanes and tropical storms.

THE HEART-STOPPING VIRUSES OF YOUTH

MINOR CHILDHOOD INFECTIONS could be leaving behind a deadly legacy: New research suggests they may sharply increase the risk of a heart attack decades later. If the findings are confirmed, antiviral drugs could become a powerful new weapon against heart disease, saving lives and lowering the $66 billion annual cost of treating such ailments.

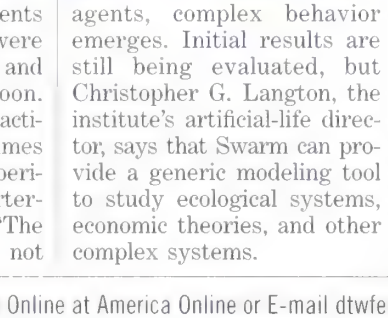
Stephen E. Epstein of the National Institutes of Health studied a common organism called cytomegalovirus, or CMV, which infects 80% of Americans by the time they reach adulthood and then persists in latent form. He found that in some people the virus becomes reactivated in artery walls, where it appears to spark abnormal cell growth that may block blood flow.

Epstein examined patients whose clogged arteries were opened by the insertion and inflation of a tiny balloon. Those with evidence of reactivated CMV were three times as likely as others to experience reclogging of the arteries within six months. "The data are compelling but not conclusive," admits Epstein. "The concept needs a year or two of testing before we move to the clinic." By then, he says, we may also understand why CMV becomes reactivated in some patients but not in others.

SOFTWARE FOR THE PAST'S PUZZLES

ONE OF THE GREAT MYSTERIES of archeology is why the Anasazi culture in the Four Corners region of the southwestern U.S. collapsed abruptly in the 12th century, despite a far-flung network of roads that supported thriving commerce. To test the various theories, such as prolonged drought or overpopulation, researchers at New Mexico's Santa Fe Institute are using so-called artificial-life simulation. The software, called Swarm, evolves its own models of the complexities of real life.

The researchers started with 3-D satellite maps of the region, then added software "agents" that model such variables as weather and agricultural yields. From this swarm of fairly simple agents, complex behavior emerges. Initial results are still being evaluated, but Christopher G. Langton, the institute's artificial-life director, says that Swarm can provide a generic modeling tool to study ecological systems, economic theories, and other complex systems.



INNOVATIONS

- A team of scientists led by Flossie Wong-Staal of the University of California at San Diego is trying to arm immune-system cells against the virus that causes AIDS. The team extracts the immune cells from patients. It then inserts into the cells a gene for a substance that chews up incoming viral genetic material. In a test tube, the cells resist HIV infection. The next challenge will be to deliver the gene widely to immune cells in the body. And the ideal vehicle may be a weakened form of HIV, says Wong-Staal. It attacks "the very cells you want to target."
- New data show that human fertility has declined in every part of the world during the past five years, according to Wolfgang Lutz of the International Institute for Applied Systems Analysis in Austria. Thanks to social development and the education of women, there is "a 65% chance that the world population will never double again," he says. He predicts that global population may peak at about 10 billion in 2050.
- Tuberculosis, now the leading killer of the world's adults, will claim 30 million lives in the next decade, says Rita R. Colwell, a biologist and president of the American Association for the Advancement of Science. TB is just one scourge the world is facing, though—and Americans aren't immune. Malaria, already ravaging Asia, could soon begin to spread across the U.S., she fears.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwfeb@businessweek.com

HERE COMES T

And it could be the simple solution to companywide information-on-demand

Businesses of every kind have found that the Internet's World Wide Web is a great way to get information to customers, partners, or investors. Now, they're finding that using the same technology internally—on intranets—can dramatically improve communications, unlock hidden information, and transform organizations.

In the brief annals of doing business on the Internet, Federal Express Corp.'s customer Web site has become a legendary success story. The package-delivery giant, which moves 2.4 million pieces every day, put up a server in November, 1994, on the World Wide Web that gave customers a direct window into FedEx' package-tracking database. By letting 12,000 customers per day click their way through Web pages to pinpoint their parcels—instead of asking a human operator to do it for them—FedEx was soon saving up to $2 million a year by some estimates.

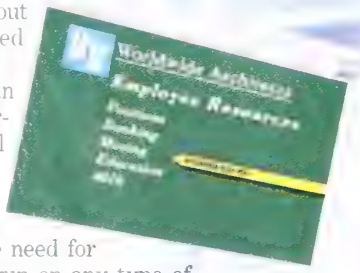
"We saw the success of the package-tracking site and said, 'Wow, I wonder what we could do on the inside?' " says Susan Goeldner, manager of Internet Technology for Federal Express. The answer: a lot. Today there are 60 Web sites running inside the company, most created for and by employees. Next, as part of a companywide Web push, FedEx is equipping its 30,000 office employees around the world with Web browsers so they will have access to a slew of new sites being set up inside the company's Memphis headquarters.

"FIRE WALLS." FedEx is not alone. After getting their feet wet with public Web sites that promote company products and services, corporations are seizing the Web as a swift way to streamline—even transform—their organizations. These private Nets, or "intranets," use the infrastructure and standards of the Internet and the World Wide Web but are cordoned off from the public Internet through software programs known as "fire walls": Employees can venture out onto the Net, but unauthorized users can't come in.

The Web, it turns out, is an inexpensive yet powerful alternative to other forms of internal communications, including conventional computer setups. One of an intranet's most obvious virtues is its ability to slash the need for paper. Because Web browsers run on any type of computer, the same electronic information can be viewed by any employee. That means all sorts of documents—internal phone books, procedure manuals, training materials, requisition forms—can be converted to electronic form on the Web and constantly updated for almost nothing.

WHAT'S NEEDED? Most companies already have the foundation for an intranet—a network that uses the Internet's TCP/IP protocol. Computers using Web-server software store and manage documents built on the Web's HTML format. With a Web browser on your PC, you can call up any Web document—no matter what kind of computer it's on.

■ Fire wall programs that run on server computers seal off the corporate intranet from the vast public Internet, keeping intruders out.



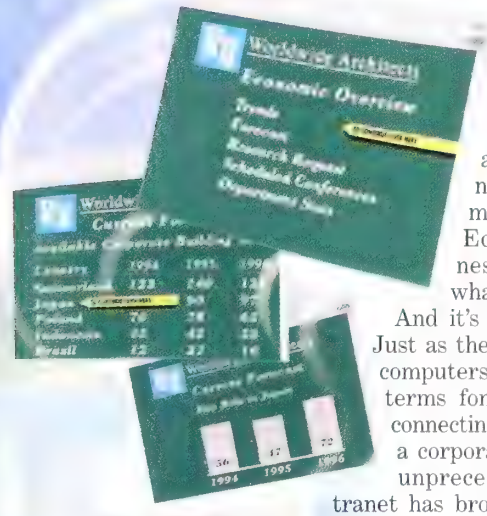
■ An engineer interested in relocating to San Francisco can search a company's internal job listings by location and skill required.

IE INTRANET

Special Report

But intranets can do something far more important. By presenting information in the same way to every computer, they can do what computer and software makers have frequently promised but never actually delivered: pull all the computers, software, and databases that dot the corporate landscape into a single system that enables employees find information wherever it resides.

Universal reach, of course, is what made the Internet grow so rapidly in the first place. But Net enthusiasts tended to focus on how to link far-flung people and businesses. "When the Internet caught on, people weren't looking at it as a way to run their businesses," says Tom Richardson, marketing manager of Digital Equipment Corp.'s Internet Business Group. "But that is in fact what's happening."



o prepare for a meeting,
executive taps into the
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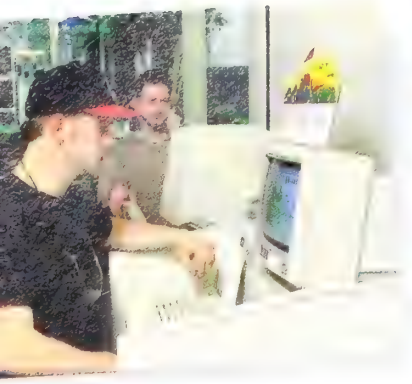
dled electronically.

And it's happening with amazing speed. Just as the simple act of putting millions of computers around the world on speaking terms fomented the Internet revolution, connecting all the islands of information in a corporation via an intranet is sparking unprecedented collaboration. "The intranet has broken down the walls within corporations," says Steven P. Jobs, CEO of NeXT Computer Inc.

From AT&T to Levi Strauss to 3M, hundreds of companies are putting together intranets. At Compaq Computer Corp., employees tap into a Web server to reallocate investments in their 401(k) plans. At Ford Motor Co., an intranet linking design centers in Asia, Europe, and the U.S. helped engineers craft the 1996 Taurus. Scientists working in fields such as genetics and biotechnology credit intranets with allowing them to share information with colleagues and quickly sift through volumes of data that might have taken days to find in the past.

Across the business world, employees from engineers to office workers are creating their own home pages and sharing details of their projects with the rest of the company. At National Semiconductor Corp., for instance, an engineer rigged a home page that lets his department schedule meetings online. "It's like a thousand flowers blooming," says Frank



Special Report

Dietrich, corporate Web systems manager at Silicon Graphics Inc., whose 7,200 employees have access to 144,000 Web pages stored on 800 internal Web sites.

All this has not been lost on the software industry, which has been reinventing itself ever since the Internet and the World Wide Web hit. At first, software makers focused on Web browsers and other programs aimed at making the Web a consumer medium. But lately, with Net commerce getting off to a slow start, software makers are chasing a more immediate opportunity in helping corporate customers build intranets.

Market researcher Zona Research Inc. in Redwood City, Calif., predicts that sales of software to run intranet servers will shoot to more than $4 billion in 1997, from $476 million last year. In 1998, Zona says the figure will hit $8 billion, four times the size of the Internet server business. And that doesn't include all the applications packages, programming tools, and other pieces that go into intranets. No wonder Netscape, Sun Microsystems, Microsoft, IBM, Oracle, Computer Associates, and nearly everybody in the software business is rushing out intranet products. "Intranets are huge," says Sun CEO Scott G. McNealy.

WAKE-UP CALL. They're tapping a ready market. Not only do corporations already have the networking infrastructure—and the money to actually pay for software—but they also crave technology that finally gets information out of the arcane world of databases into a format anyone can use (page 82). A survey by Forrester Research Inc. of 50 major corporations found that 16% have an intranet in place and 50% either plan to or are considering building one. "People woke up one morning and realized they had all the pieces in place," says Paul D. Callahan, director of the researcher's network strategies service.

The intranet provides an opportunity for software makers to revitalize their businesses and another chance for companies that were left behind by previous techno-trends to get ahead. But it also poses a big threat to dozens of companies and products. Suddenly, the Web provides a simple way to do things that in the past required gobs of complex code and specialized programs. The first company to find this out was Lotus Development Corp., which has had to defend its Notes program—a powerful system for helping workers collaborate across networks—in the face of cheaper Web alternatives.

Notes may be just the first product to feel the squeeze. Companies such as SAP, the $1.9 billion German software maker, have risen to the top ranks of the industry with complicated programs to paper over the differences among computer systems. Now, at least in theory, the Web can do much the same job—faster and for a lot less. "The question is, should we wait [for SAP] or do something with the Web?" says Todd Carlson, chief information officer at Electronic Data Systems Corp., which has begun a two-year, multimillion-dollar deployment of enterprise software from SAP in Europe but is considering using the Web to get at some of the same data.

It's not just the cost of buying Notes or SAP's R/3 and paying programmers to customize and maintain it. The other factor tipping the scales toward the intranet approach is the cost of training. Not only has the Web's HTML (hypertext markup language) standard emerged as a universal electronic communications medium but it also serves as a standard user interface. By now, millions of PC users have become familiar with the drill: Click on a blue, highlighted word or a graphical button and jump to another Web page. To retrace your steps, simply click on an arrow at the top of the screen. All Web pages, no matter what their appearance, work this way. It requires little if any training—and makes finding electronic information simple enough for everyone in a company.

Another plus for intranets is the relatively low cost of ownership. Because the same basic programming can be used on lots of different kinds of hardware, corporations will need fewer programmers to write and maintain software.

Intranets, however, aren't the magic bullet for every software ill. Nothing on the Web can replace the complex business programs that have been refined over many years—yet. And companies may still opt for the unimpeachable security of conventional programs.

But software makers have seen the handwriting. As Lotus is doing, companies such as SAP are adapting their products for the Web—before Web

The Web Warriors

NETSCAPE The red-hot startup has a big lead in browsers, and its server programs are catching on. Can it stay ahead?

MICROSOFT The software giant is building Net capabilities into all of its software programs: Windows NT, for example, will include Web "server" software bundled for free. That could appeal to customers—and put pressure on rivals.

IBM The company's Lotus subsidiary is remaking its Notes groupware program into a Web-friendly program that will be the centerpiece of IBM's Net push.

SUN The company is selling lots of Web server computers. Now its Java language promises to usher in a new generation of dynamic Web applications.

NOVELL Its Netware program still runs most local-area networks, but the networking king could blow an opportunity to lead on the Web.

CALLING UP THE BENNIES: *At a Compaq factory in Houston, workers check on their benefits, savings, and 401(k) plans at a kiosk hooked into the intranet*

pstarts begin to encroach. "It will become increasingly important for SAP and others to 'webize' their software," says J. Neil Weintraut, an analyst with Hambrecht & Quist. "In ve years, the term Web software will be redundant."

For now, most intranet Web sites are used for basic information sharing: publishing job listings, benefits information, nd phone directories, for example. Some of these simple information-sharing setups already provide strategic advantage, hough. Cap Gemini's Knowledge Galaxy is a giant repository f technical information that helps the consulting firm repond more quickly to customers, for example (page 83).

More sophisticated intranets are coming. They will let employees fill out electronic forms, query corporate databases, or old virtual conferences over private Webs. Corporate information systems managers are "just now seeing [the Web] as he next step in application development and distribution," ays Greg Sherwood, National Semiconductor's Web coordinator and chairman of the chipmaker's World Wide Web council.

For a taste of the future, check out Silicon Graphics. The maker of high-end graphics workstations began using the Web internally almost as soon as Mosaic, the original Web browser, was born. The company started out with the basics—publishing information electronically and making it available to employees at the company's Mountain View (Calif.) headquarters and around the world. Today, says Dietrich, "there's barely a piece of information that's not online."

But Silicon Graphics didn't stop there. Using its intranet, dubbed Silicon Junction, the company today accomplishes such feats as making accessible more than two dozen corporate databases that employees can traverse by clicking on bright-blue hyperlinks. Previously, to get the same information, an employee had to submit a request to a staff of specially trained experts who then would extract the requested data from the company's databases—a process that could take several days.

SGI also regularly sends video and audio feeds to employees around the world on the Net. When President Clinton visited SGI's headquarters in February, 1993, employees around the world tuned in via the intranet. "We're using the Web to expand the horizons of all of our employees," says Dietrich.

Most people don't work at a place where they put an

DREAMWORKS

It's a Wrap–With the Intranet

The high-profile triumvirate of Steven Spielberg, Jeffrey Katzenberg, and David Geffen announced in October, 1994, plans to create a new entertainment powerhouse: DreamWorks SKG. Their aim: to create the digital entertainment studio of the 21st century. Their first project: an animated feature film, *Prince of Egypt*, slated for the 1998 holiday season.

Putting together a system to make that happen is the job of another, less well-known trio. They are Dylan Kohler, Rob Hummel, and Bill Villarreal, technology coheads for DreamWorks' animation division. Known as the "three amigos," they set to work last spring on an equally state-of-the-art production-management system to coordinate the project's many facets. "We had an entire system to build—plus trying to do a movie," recalls Kohler.

In one sense, they were lucky: They didn't have any "legacy" computers to deal with. Still, they had to make sure the production system could work with an eclectic assortment of whiz-bang workstations and animation programs. And the amigos had no time to lose.

"THREE AMIGOS": *Kohler, Hummel, and Villarreal co-head the animation division*

If they used a conventional client-server setup, they realized, they would have to spend time and money writing programs for many machines. With an internal Web and Netscape Communications Corp. browsers on each desktop, they avoid "the dirty work of doing a lot of client applications," says Kohler.

The system, which is called Nile, will be available in March to 100 production managers and artists. It will be used to check on the daily status of projects, track animation objects, and coordinate scenes. NEXT Computer Inc.'s WebObjects will handle the queries and fetch information.

Eventually, Kohler says, the intranet will be used throughout the company in the production of live-action films, music, TV shows, and new media being developed at DreamWorks Interactive. Best of all, the entertainment studio can grow with it. The Web, says Kohler, "is an evolving architecture. And that's what DreamWorks is all about."

By Amy Cortese in New York

IMAGINE *building a Web site that really means business.*

Every day, more businesses are creating their own Web sites. To set your business apart, you need a site that communicates effectively. At the same time, it should be cost effective to create and maintain.

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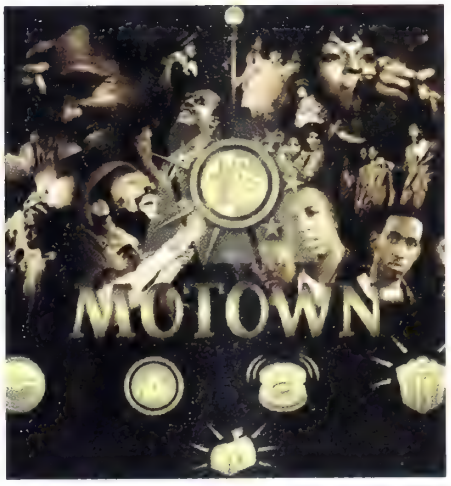

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$5,000-plus workstation on every desk. But the same capabilities that Silicon Graphics employees enjoy now are coming to ordinary desktop PCs.

The challenge—and opportunity—for the software industry is to come up with programs and Web-development tools to make such sophisticated intranet applications possible at all sorts of companies. The first requirement: "tools" that make it possible for anyone to create Web content. The HTML format, the lingua franca of the Web, can be clunky. So software makers are flooding the market with programming packages that mask the complexities of HTML. The market for Web-authoring tools was just $2 million last year. It will hit $300 million by the end of the decade, predicts Hambrecht & Quist.

THE NEXT STEP. Electronic publishing pioneer Adobe Systems has sold more than 30,000 copies of PageMill, an HTML-authoring tool, since December. Microsoft has given away thousands of copies of Internet Assistant, a program that converts Word documents to HTML, and is readying an update to Microsoft Office with built-in HTML authoring. On Jan. 16, it acquired Vermeer Technologies Inc., a startup that makes easy-to-use Web tools, for an estimated $130 million.

The next step is software to take the Web beyond static pages. Today, most pages contain canned information that can be viewed but not manipulated. With the right programming, however, a page can become interactive—an easy-to-use, fill-in-the-blank system for database queries, for example.

Some leading-edge companies, including SGI, Federal Express, and EDS, have already built such setups. But they had to hand-code the database links in an esoteric language called "perl." Software makers are now coming up with programs that will make it much easier to assemble custom Web applications that can work with existing systems. Steve Jobs's NeXT, for example, has a new line of programs called WebObjects, which can crank out custom Web pages on the fly. That's helping companies such as DreamWorks SKG quickly get intranets up and running. Computer Associates International Inc., the $3 billion supplier of systems software, has a program called Jasmine that, like NeXT's WebObjects, uses object-oriented software to create custom Web applications.

In terms of Web buzz, nothing tops Java, the promising programming language developed at Sun Microsystems. Java provides a way of writing small software "applets" that can be zapped across the Net to do little tasks such as calculating an expense report or displaying fresh stock prices. Companies including Borland International and Symantec Inc. are coming out with development "environments" for Java. Sun itself is drafting extensions to the programming language that enable Java programs to fetch data from corporate databases, making it suitable for all sorts of corporate applications, says Alan Baratz, president of Sun's JavaSoft unit.

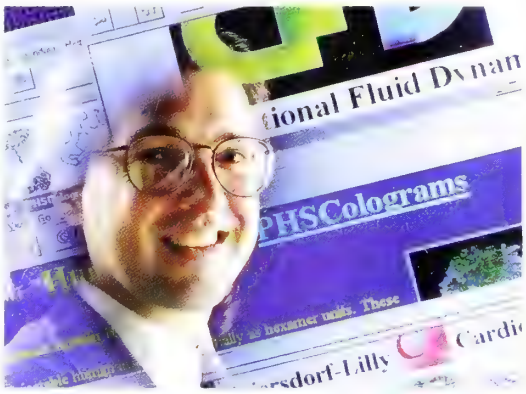
Because of their sealed borders, intranets are ideal for testing the idea of electronic distribution of software—Java applets or updates of entire programs. Many companies are already putting applets and other bits of software on internal Web sites so they can be shared by programmers. At Hewlett-Packard Co., software writers now check what's in a "software vending machine" before writing new code.

Not surprisingly, the intranet is a magnet for startups. Much of the entrepreneurial energy is focused on meshing Web systems with existing systems. Spider Technologies has a program that lets companies graphically link their databases with Web sites. Maximum Information Inc.'s WebC family of programs help corporate software developers integrate Web systems into existing computer setups. Another newcomer,

ELI LILLY

Oh, What an Untangled Web

When information consultant John Swartzendruber saw the simple way the World Wide Web conveys information, he had a vision of how that could change things for his employer, pharmaceutical giant Eli Lilly & Co. "I was struck with all the kinds of data you could get at with just one interface," he says. Swartzendruber sold management on his vision and last year hooked up 3,000 desktops in two dozen countries. By the end of 1996, Lilly's intranet will link some 16,000 workers—almost two-thirds of its worldwide staff.



CYBERVISION: *Swartzendruber hooked up 3,000 desktops in two dozen countries last year*

Already it has simplified tasks such as scheduling clinical trials and submissions for new drugs in 120 countries. Typically, each market has unique requirements on how trial data must be collected, analyzed, and labeled. Before the intranet, teams of research administrators, physicians, statisticians, and legal experts relied on fragmentary information and guesswork to choose trial sites. Regulatory information from different countries had to be laboriously assembled via E-mail, causing deadlines to slide.

The situation was maddening because all the required information existed somewhere in the company—if one only knew where to look. Now, the intranet brings it all to a series of Web pages. "The regulatory person at a meeting can refer to a page on the Web and take the whole group through the process step-by-step," says Diana McKenzie, an information technology manager in charge of regulatory affairs. A planning team in Indianapolis can skip across time zones to databases on far-flung servers without waiting for colleagues on different continents to punch in. That way, it can tell in minutes whether the preparation time for a given market will meet management's schedule. "We find everything out at the planning session, before it's too late," McKenzie says.

"Groupware" products such as Lotus Notes could do all that—but only after considerable outlays of money and time for training and support, says Michael C. Heim, an information officer for Lilly Research Laboratories. For people simply reviewing and sharing data, he says, "Notes gives you more complexity than you need." Indeed, Swartzendruber linked Lilly's first 3,000 intranet acolytes for just $80,000. "Intranets aren't the Holy Grail of computing," he says. "But for now, they're hard to beat."

By Neil Gross in New York

HAHT Software Inc., makes a development tool called HAHTSITE for Web systems that can pull information from corporate databases. And Edify Corp. and Business@Web both aim to ink companies' business applications, such as customer service or sales, with the Web.

The Web is still not suited for "mission-critical" applications such as order processing or accounting. But in the high-speed world of Internet development, that may not be true for long. Gradient Technologies Inc. in Marlboro, Mass., and WayFarer Communications in Mountain View, Calif., are two startups working on that challenge. The basic problem, says WayFarer CEO Edward Colby, is that Web servers weren't designed for high-speed transactions, things like getting a credit authorization. WayFarer's QuickServer uses its own messaging protocol to speed up transactions (basically messages between databases) and juggle high-volume database requests.

When the fledgling software companies talk of mission-critical computers, they're aiming at the entrenched home markets of the giants: IBM, Sun, Digital Equipment, and Microsoft. For now, at least, the odds are heavily in favor of the incumbents. Consumers surfing the Web may gamble on the latest software they can download. But corporations want to know that they're getting their intranet technology from someone they can trust. John Whiteside, head of IBM's Global Network, hopes to translate that sentiment into a billion dollars in business this year. "Every single one of our customers is asking for something in terms of an intranet," he says.

Companies such as Oracle and Sybase Inc., which make powerful database systems—the lifeblood of a corporation—are also well-positioned. Sybase is testing a program called Web.SQL, which links Web servers with databases from Sybase and others, and Oracle is set to release new server and database programs for the Web.

Longstanding customer relationships give the big guys a foot in the door, but they have to deliver the goods, too. That's why Microsoft is now focusing all its energies there—especially on the intranet segment, where it needs to succeed to hold on to its lead in operating systems and applications. Declaring in December that "the sleeping giant has awakened," Microsoft executives unveiled a broad Internet effort.

This month, Microsoft made a splashy entry into the market for Web-server software, the basic programs for intranets. Until now, the Web software market has operated on a novel formula: Companies charge little or nothing for the basic browser program and make up the difference by charging full fare for server programs. Microsoft, however, is giving away both its Internet Information Server program and its browser on the Net. The server software will also be bundled at no extra cost with Microsoft's Windows NT operating system. Dozens of computer makers, including Compaq, HP, and Digital Equipment, plan to ship the software with their servers. "Basically, we're gonna drop this thing from airplanes," says James E. Allchin, senior vice-president of Microsoft's Business Systems Div.

Special Report

The carpet-bombing could quickly turn Microsoft from an Internet laggard to an Internet leader. After two years, Windows NT has become a leading operating system for the kind of small-scale servers used on local-area networks. Now, those machines are likely to become intranet servers, too. In addition to basic Web server software, Microsoft's free In-

CAP GEMINI

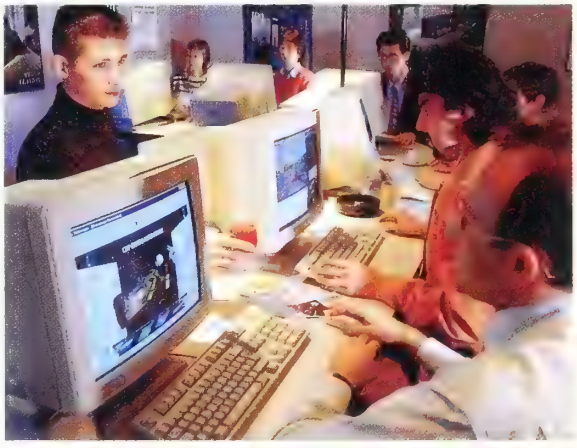
One Electronic SOS Clinched the Deal

It didn't take long for French computer-services giant CAP Gemini Sogeti to find out the value of the intranet it installed last September. Project manager Ed Baugh's customer, Exxon Chemical Co., wanted a software-development tool that would help it blend off-the-shelf software packages with the oil giant's custom business applications. Exxon had combed the market for five months in vain. And Baugh knew building the tool from scratch would take at least 18 months, too long for Exxon's needs.

Hoping CAP Gemini's 17,000 software engineers and technicians might have a lead, Baugh sent out an electronic SOS across the company intranet, dubbed Knowledge Galaxy. Presto—48 hours later, CAP Gemini's British unit, Hoskyns Group PLC, responded. An engineer there knew of a software tool that might be tailored to meet Exxon's needs. Within three weeks, Baugh presented a solution to Exxon and clinched a hefty development contract. "We found the missing link," says Baugh.

Knowledge Galaxy has helped CAP Gemini cut project time in half and prepare sales bids faster by putting critical resources and expertise within every employee's reach. As a virtual storehouse for software objects, or prefabricated chunks of code, it has helped the company avoid reinventing the wheel for each project. "We now reuse objects like Legos," says Jean-Paul Figer, group vice-president in charge of developing CAP Gemini's intranet.

The consulting company's network is more than just an elaborate E-mail and filing system. It has areas for electronic chats and bulletin boards, a database of current projects with links to employees working on them, and hundreds of Web pages aimed at keeping a global workforce up to date on the latest technologies. CAP Gemini is so enthused with the Web it has set up an Internet café for employees at its Paris headquarters so they can surf the Net while on break.



MISSING LINKS: *Workers at CAP Gemini's Paris headquarters lounge in the company's Internet café*

CAP Gemini hopes to do lots more on its intranet. First, however, it has to solve a problem plaguing both high- and low-tech companies: getting people to use it. "The real challenge is to change behavior," says Figer. Success stories such as Baugh's will certainly help.

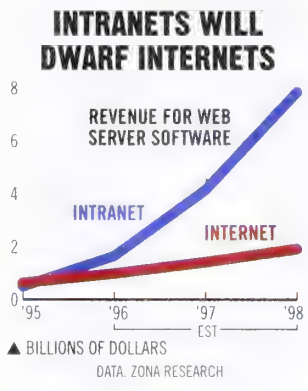
By Gail Edmondson in Paris

ternet Information Server includes security features and the ability to connect to corporate databases.

That has sent an alarm across the industry. Microsoft's tactics—it is building Web capabilities into all of its programs—could really shake up the Web software market just as companies are starting to make money. "Microsoft has spoiled the party," says Forrester Research's Callahan. The decision to give away the Web server "was a masterstroke" and "a crushing blow" to rivals, he says. Microsoft insists that building in the server program is not sinister but part of the natural evolution of operating-system software. "We view it as a native part of the [operating system]," says Allchin.

Still, Microsoft's Net plans have raised the interest of the Justice Dept. As part of an ongoing investigation into the company's business practices, Justice lawyers are looking into Microsoft's acquisition of Vermeer. "We're quite confident they'll realize there is no issue there," says Pete Higgins, a Microsoft group vice-president.

Who will be hurt by Microsoft's Net push? Netscape, which charges a few hundred to a few thousand dollars for server programs, is the obvious target. The company's stock sank $4, or 6%, on Microsoft's Feb. 12 announcement. But Netscape is not as dependent on server sales as it had expected to be. To build intranets, companies are installing thousands of copies of the Netscape Navigator browser—and paying for them so they get customer service. And because Navigator is the de facto standard, analysts expect strong sales to continue, despite Microsoft's browser giveaway.



Netscape shrugs off the challenge from the north. "It has not impacted our sales," says co-founder Marc Andreessen. Still, Netscape is running as fast as it can. It is rushing out new versions of its Web-server programs—with new pricing—next month. And the latest update of Navigator adds features such as "frames," a Windows-like way to display multiple pages on a screen, E-mail, and built-in security to validate a user's identity. It also includes a scheme for plugging in companion programs, such as Adobe's Acrobat document viewer and Progressive Network's audio player, to round out the browser's features.

A HORSE RACE. At the same time, Netscape is pushing into new areas that will appeal to the intranet crowd. Last September it bought Collabra, a maker of groupware programs that have some, but not all, of the capabilities of Lotus Notes. And on Jan. 31, Netscape said it would acquire InSoft Inc. for around $160 million. InSoft's technology enables teams to collaborate via audio and video over the Net and will lay the foundation for Netscape's LiveMedia, an industry-supported framework for delivering real-time, multimedia services over the Web.

Can Netscape keep ahead when dozens of startups, Microsoft, and everybody else in the business is on its heels? Maybe not. But it certainly makes an enjoyable spectacle for corporations planning their futures around intranets: Hundreds of rivals striving to come up with better Web software can only make those intranets come to life sooner. As the man said: Let a thousand flowers bloom.

By Amy Cortese in New York with bureau reports

Special Report

VISA INTERNATIONAL

Updates? Just a Mouse Click Away

When the Internet and the World Wide Web exploded into the corporate consciousness last year, Visa International Inc. executives Cathy Basch and Deborah McWhinney saw an opportunity. "We got to thinking maybe there was a way to take advantage of that technology to do things in a faster, cheaper, and better way," says Basch, who is senior vice-president in charge of VisaVue, the company's information service for member banks.

Basch and McWhinney, senior vice-president for information products, helped the financial services company put all sorts of information on an internal Web site: employee directories, newsletters, even cafeteria menus. The electronic directory alone was a boon. Before, to keep Visa's 1,200 employees informed about who was the right contact for each of 19,000 member banks, Visa regularly published two volumes, each nearly four inches thick—and each instantly out of date. Now, the latest information is a few mouse clicks away. "It makes all the difference," says Basch.

Visa's intranet has been such a hit that the company is now looking at creating a separate network for member banks. Today, the company sends out most information—such as fraud alerts and marketing updates—on diskettes. By putting that online, Visa will not only speed things up, it will also be able to offer more services, and let banks tap directly into its databases—to check the status of a transaction electronically, a process done manually today.

McWHINNEY AND BASCH: *Their intranet may lead to one offering services to member banks*

Creating intranets that extend to customers is a risky but potentially profitable development. Venturing beyond the corporate fire wall introduces security risks, and Visa is holding off until it can be sure its data will be safe. But the company is eager for the payoff: greater efficiency for itself and better service for the banks. And in a cutthroat business such as Visa's, says McWhinney, that kind of advantage is hard to pass up.

By Amy Cortese in New York

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ARTHUR ANDERSEN

INEQUALITY

IS AMERICA BECOMING MORE OF A CLASS SOCIETY?

New data show that, increasingly, workers at the bottom are staying there

Keith Mahone thought he was going places after he graduated from high school and landed a mail-room job at *The Baltimore Sun* in 1983. True, it only paid the minimum wage, but Mahone figured he could move up if he did well. He did move during the next six years—but only to purchasing, the stockroom, and other low-skill jobs that paid just marginally more. Fed up, the Baltimore native quit in 1989.

Mahone, now 36, has been hustling ever since to get ahead in today's high-skills economy. He enrolled in a year-long training course to become a cable-TV technician. But when he finished, cable companies offered him the same $6-an-hour installer job that he could have had without it. After that, he grabbed any job he could, at a food distributor, an incense factory, a meat packer, and as a school custodian. All paid $4 to $6 an hour and ended when the employer closed or laid him off. "These low-wage jobs trap you and take away your hope," Mahone says angrily. "They have no opportunity to further yourself. I always thought mopping the floors was for lazy people, and I never in all my dreams thought I would be doing it. It's hell to fight your way out."

WIDER GAPS. As long as the country's Keith Mahones had the chance to work their way out of the bottom, Americans have tolerated wide gaps between rich and poor. After all, the U.S., unlike more rigid economies in Europe, has always been dynamic enough to provide steady upward mobility for workers.

Now, a spate of new research on U.S. income mobility suggests that America is shutting out more people like Mahone. A dozen or so academic studies have examined data that follow the same individuals for many years. This allows them to go beyond research showing rising income inequality to reveal a more unsettling trend: As the economy stratified in the 1980s, workers at the bottom became less likely to move up in their lifetimes. At the same time, upward mobility is increasing for some higher-end professionals and college-educated workers whose skills remain in high demand.

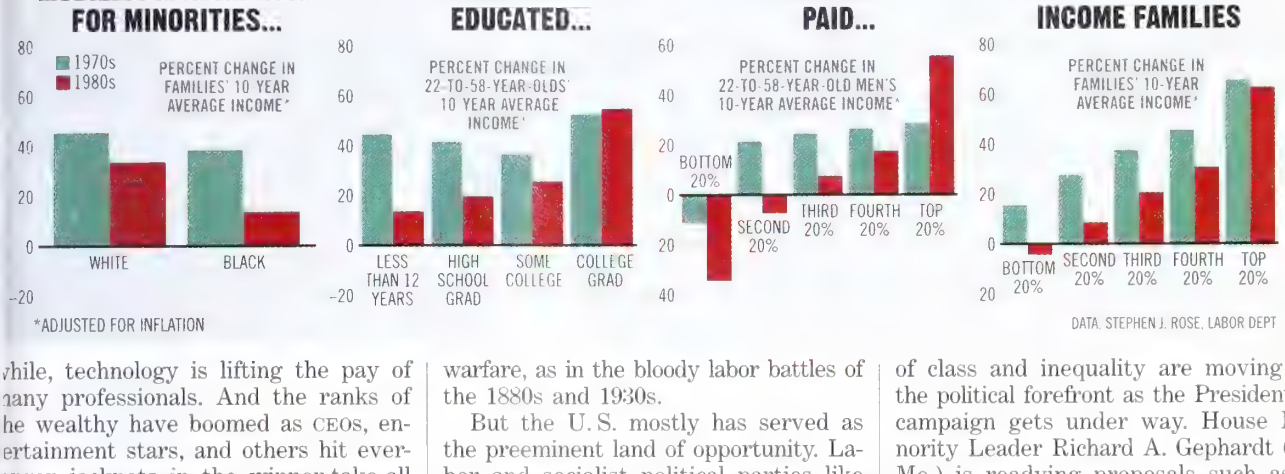
This splintering is something new in America, suggesting that our economy is becoming more rigid and class-bound. Unlike past decades, when opportunities for advancement existed at all levels, America today is cleaving into economic camps divided largely by education. Those born in families and neighborhoods that provide the money and motivation to help them complete college are more likely to get ahead. Those, like Mahone, who lack the access or the ability to achieve high skills are increasingly likely to sink, no matter how much they hustle.

"In the past, companies could hire unskilled people and train them into skilled jobs," says Henry B. Schach the former CEO of Cummins Engine C who now is chairman of AT&T's $20 bi lion equipment unit. "My predecesso at Cummins moved from the shop flo and ended up as president." But be cause Cummins, like many companie has cut many first-line managerial job "today those stairs don't exist."

The new studies raise troubling is sues about the U.S. economy. Globa competition, declining unions, and grow ing immigration have inflated to mo than a quarter of the workforce the ca dre of workers whose earnings fall be low the $15,000-a-year poverty line. An that doesn't count many of the 5% t 10% of the population in the urba underclass who don't work at all. Mea

A Land of Diverging Opportunities

Previous studies of economic inequality show changes in wage levels, but they don't follow individual workers as they move up job ladders over time. Now, new studies track the same individuals over 10-year periods to see how many moved up:



While, technology is lifting the pay of many professionals. And the ranks of the wealthy have boomed as CEOs, entertainment stars, and others hit ever-larger jackpots in the winner-take-all pay system of some professions.

These trends strike at the core of America's self-image as a classless society. Of course, we never really lived up to that ideal. Women largely were excluded from the economic market for hundreds of years, and slavery and racism meant that blacks never even had a chance until the 1940s. Gaping rich-poor chasms also ignited periodic outbursts of something very much like class warfare, as in the bloody labor battles of the 1880s and 1930s.

But the U.S. mostly has served as the preeminent land of opportunity. Labor and socialist political parties like those of class-conscious Europe never flourished here. What matters in our political culture is not equality per se but an economy and society accessible to all. This bedrock belief is a key reason why the U.S. has been a beacon for Europeans and others fleeing stratified societies.

If the new studies are accurate, the U.S. is in danger of losing the openness that underlies its democratic identity. One of the most astounding conclusions of the research is that mobility for low-income Americans is no greater today than for poor Europeans. "You can't take solace anymore in the American dream of working hard and migrating up through society," warns William J. McDonough, president of the Federal Reserve Bank of New York. "That still exists in our society, but we're kidding ourselves if we don't realize that the degree of stickiness of people in lower earnings levels is a new problem."

An increasingly class-segregated economy could one day hurt America's stable, centrist society. Already, the concepts of civic society and collective responsibility are fraying, as frustrated taxpayers lash out at Washington as the emblem of economic decline. Issues of class and inequality are moving to the political forefront as the Presidential campaign gets under way. House Minority Leader Richard A. Gephardt (D-Mo.) is readying proposals such as a minimum wage hike and tax breaks for companies that protect workers from layoff. Clinton is pushing a package of "economic security" proposals, from health insurance to strengthened pension protections. And Republican candidate Patrick Buchanan's fiery appeal to anxious workers has pushed front-runner Bob Dole to attack low wages and high profits, too.

It's possible that the economic trends underlying these problems are on the wane. Some experts believe U.S. companies have launched a productivity revival that will lift incomes and living standards across the board. It's also true that the children of blue-collar families have flocked to community colleges seeking the education required for today's marketplace.

Still, these forces may not suffice to improve pay for the less skilled. True, college enrollment boomed in the 1980s. But the share of workers with degrees grew more slowly than in the baby-boom 1970s. The resulting skills scarcity increased demand for college grads while shutting out the less skilled. That scenario is likely to continue through the 1990s, since the baby-bust generation is too small to fill the skills gap. "I keep asking people to tell me a hopeful scenario about low-skilled workers in the 1990s, but I never hear a convincing one," says Syracuse University economist Timothy M. Smeeding, who has done some of the recent mobility studies.

Indeed, the new statistics are a powerful wake-up call. Prior inequality studies rely on Census Bureau surveys that

ROAD TO NOWHERE

"I'm supporting us and... going under more and more every week"

— LAWRENCE J. SCHABOW, Truck driver for Pony Express

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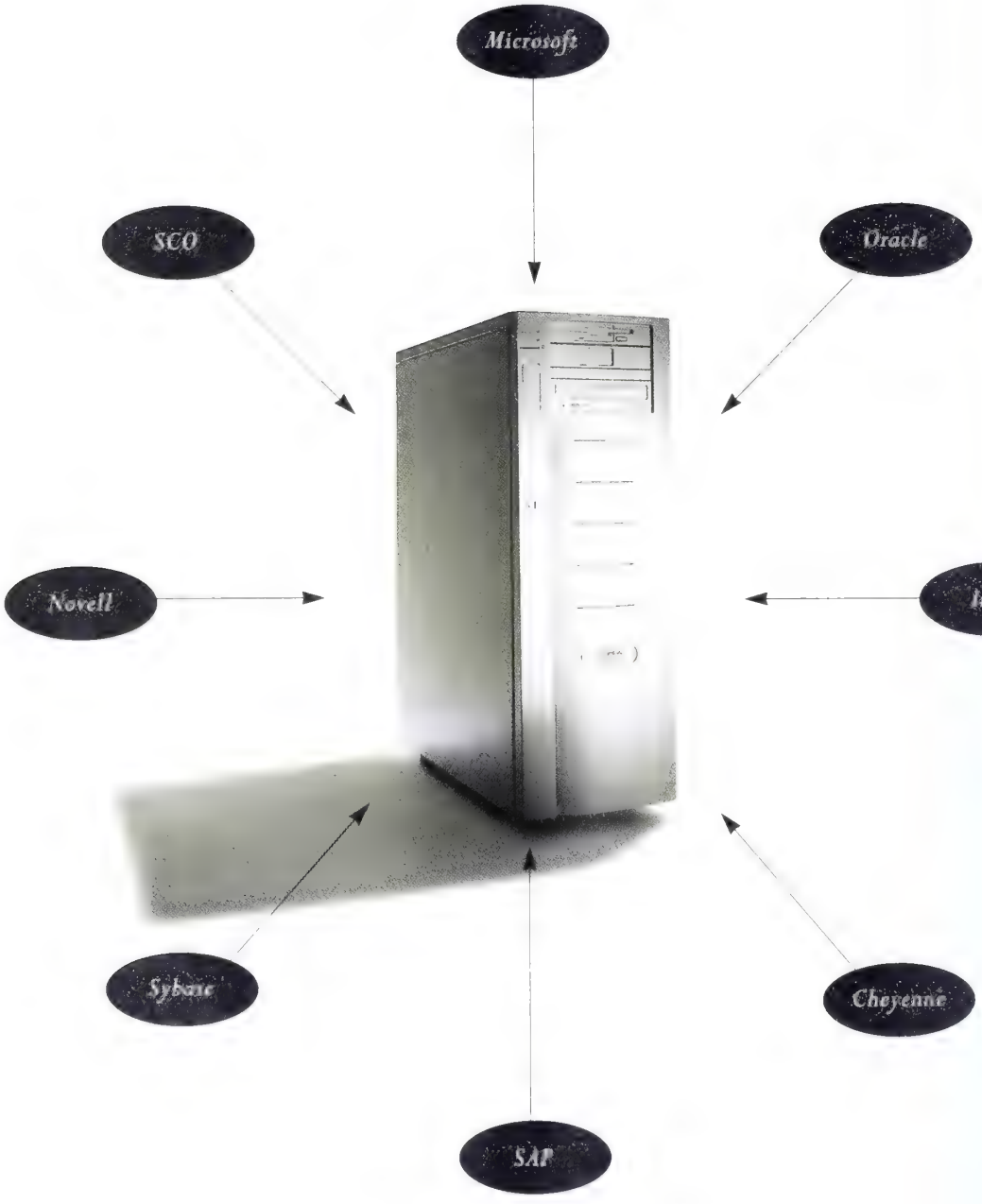

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COMPAQ

Has It Changed Your Life Yet?

take an annual snapshot of the economy to determine how much each worker earns. But the surveys don't follow the same individuals over time, so they can't show whether today's low earners were in the same boat last year.

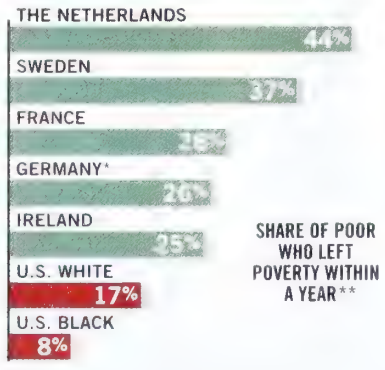
The new studies trace long-run mobility using a University of Michigan survey that has followed a nationally representative sample of 5,000 families since 1967. Stephen J. Rose, now a Labor Dept. economist, started with men and women who were 22- to 48-years-old in 1970 and tracked their earnings every year of the decade. He did the same with adults in the same age group in 1980. Since many individuals' annual earnings fluctuate a lot, Rose computed each person's average earnings, adjusted for inflation, over all 10 years of each decade.

SPLINTERING. The results show that mobility has diverged sharply over the 1980s vs. the 1970s. Consider the results when measured by education levels. In the 1970s, the 10-year earnings of high school dropouts and graduates progressed at 45% and 42%, respectively. This was roughly the same as the 53% improvement in living standards that college grads saw, Rose found (charts, page 87). In the 1980s, however, less educated workers moved up much less than more educated ones. Dropouts' 10-year average crept along at only 14%, high school grads by 20%, while college grads continued to advance at a 55% pace.

Decreasing mobility out of the bottom is even clearer by wage levels. Using the same definitions he employed for education, Rose found that men in the bottom fifth of wage-earners began to fare badly even in the '70s, when their 10-year average pay lagged inflation by 11%. But they fell out of bed completely in the '80s, losing 34%, the Michigan data show. By contrast, men in the top fifth saw their 10-year pay soar by 56% in the '80s, nearly twice as fast as their 29% gain in the prior decade.

The upward movement of families has splintered, too. More working women since 1970 helped many families offset the slump in men's earnings. But because people tend to marry at their own earnings level, low-income families have gained less. More poor families also are headed by single parents. Throughout the 1970s, though, the average inflation-adjusted incomes of such families still advanced by 16%, Rose found. But the ride ended in the 1980s, and families in the bottom fifth moved down the economic ladder by 4%.

Meanwhile, the upper fifth scored 60%-plus gains over both decades. "When you use long-term averages to



TRY, TRY AGAIN

"These low-wage jobs trap you and take away your hope"

— KEITH MAHONE, Frustrated worker

get rid of people who are only temporarily rich or poor, you can see that mobility has declined" at the bottom, says Peter T. Gottschalk, a Boston College economist who has studied mobility. Indeed, diverging mobility has shriveled the middle class—$15,000 to $50,000 a year in today's dollars—from 61% of families in 1969 to 50% in 1992, according to the Economic Policy Institute (EPI), a Washington think tank.

REVERSAL OF FORTUNE. The collapse of upward mobility at the bottom is so surprising because even the most skeptical experts believe that nearly everyone gained ground in prior decades. The annual wage figures from Census show that the incomes of families in the bottom fifth actually rose faster—2.95% a year—from 1947 to 1973 than those in the top fifth, whose incomes climbed by 2.48% a year. These numbers don't indicate how many families remained in one group or the other during this period. But even if a family had remained stuck at the very bottom for the entire 25 years, its inflation-adjusted living standard would have doubled. "No one would argue with the idea that mobility was higher in the '50s and '60s," says Christopher J. Frenze, a Republican-appointed economist at the Joint Economic Committee of Congress.

Even more astonishing, American mobility now looks worse than Europe's (chart). In 1993, Northwestern University economist Greg J. Duncan and seven European economists found that throughout the 1980s, only 17% of poor American families moved at least 20% above the poverty line within a year vs. 25% to 44% of the European poor. Overall, more than 56% of the bottom fifth American families remained there for at least five years, vs. 52% in Germany, according to Syracuse economist Douglas Holtz-Eakin. "Most economists simply can't believe that the U.S. has the same mobility as Germany," says Richard Burkhauser, a Syracuse economist who also has studied mobility with

e Michigan data. "Everyone always ought that people don't move nearly much there."

Nor do the 1990s seem to be turning much differently. The Michigan data available only through 1991. But individual workers' long-run progress is ven largely by the pay rates of the s they get. And these figures, available from Census through 1994, show same inequality patterns of the '80s. r instance, hourly pay for men in the ttom fifth trailed inflation by more an 5% from 1989 to 1994, according to EPI. Male dropouts' wages plunged 11% over this period, ile high school grads pped nearly 4%. This strong circumstantial idence that anyone o hasn't returned to hool or received subntial training likely sn't seen much of a y hike in this decade. While higher-educat- workers have fared rse compared with 1980s, they're still tpacing bottom-end es. Pay rates for men the top fifth fell by ly 1% from 1989 to 94, the EPI found, and se for men with colge degrees slumped just 0.4%. Since the lower-skilled did en worse, the gap between the two ups has widened again. Technological vances eventually may boost wages the college-educated. But numbers eased in mid-February show that in 94, the workforce as a whole got its vest raise in 14 years. And given the ntinued decline of low-end pay rates, ere could actually be even less mobil- for low-skilled workers in the 1990s an in the 1980s," says Smeeding.

INSURED. The treadmill to nowhere 't news to Lawrence J. Schabow. The -year-old Chicago resident saw his y jump from $4 an hour when he rted in 1978 as a truck driver for ny Express Courier Corp. to $10.50 in 33. Then Borg-Warner Security Corp. ught the company and began cutting ges. Today, Schabow earns $9.50 an ur, including a premium for driving at ght. That's 22% less, in real terms, an his 1983 pay. His wife, Edna, quit r clerical job in 1992 after a liver nsplant. The family pays for its own ntal and eye care after Pony ended insurance programs. When the habows couldn't pay their debts, they clared bankruptcy in 1992. "I'm supporting us and our three kids and going under more and more every week," says Schabow.

Economic opportunity has been shrinking for long enough now that families trapped at the bottom are beginning to show the attributes of a permanent lower class. Look at emergency food aid, now a nationwide enterprise. Chicago's Second Harvest, the U.S.'s largest food-relief agency, provides donated food to 185 distributors around the country, which, in turn, supply 70,000 soup kitchens and food pantries. The kitchens serve 26 million people a year, about 10% of the population.

FOOD-BANK FIX

> "I wouldn't have enough...if I had to buy all our food with my paycheck"
>
> — KARYN L. OCHELTREE, Single working mother of four

The need for food aid has risen as opportunities for bottom-end workers have declined. In Spokane, Wash., some 27% of soup kitchen users were employed in 1995, vs. 12% in 1987, according to the Spokane Food Bank, which supplies food for 33,000 households a month. Some recipients may not really need free food. But most kitchens demand pay stubs, welfare checks, and other documents. "It used to be that food service tided you over when you lost a job," says Second Harvest President Christine Vladimiroff. "But now it's chronic, because there are more working poor who can't pay the rent and still buy food."

That's the case with Karyn L. Ocheltree, a 33-year-old single mother of four who has used the Spokane Food Bank off and on for several years. In 1987, the high school graduate lost her $12,000-a-year position as an accounts-receivable clerk when the software company she worked for upgraded her job. She found similar work at another company for four years but was replaced by an $8,000-a-year trainee.

Ocheltree then enrolled full-time in a community college to study business administration, working part-time for the college and collecting food stamps and welfare to support her kids. She also took home groceries from the food bank about once a month. She landed a new job in the invoice department of a hardware distributor last July, after completing an associate's degree. But she still earns only $16,800 a year and sometimes taps the food bank. "My family eats $400 to $500 a month in food, and my rent is $550, so I wouldn't have enough left for electricity, water, and all the necessities if I had to buy all our food with my paycheck," says Ocheltree.

The U.S. has been a country of opportunity since its inception. During the 1787 drafting of the U.S. Constitution, Governor Morris of Pennsylvania argued that those whose livelihoods relied on an employer weren't independent enough to be free citizens and shouldn't vote. Thomas Jefferson later responded that Morris' point may have been valid for Europe's dirt-poor wage-earners. But Americans, he said, could always find another job or earn a decent living on the abundant farmland here.

The middle class that began to emerge in the early 1800s has provided the stable underpinnings to our democracy. But if America continues to stratify, "you'd expect our democratic identity to diminish," says political science Professor Carey McWilliams of Rutgers University. Some trapped on the bottom may explode with resentment. Others may succumb to apathy. Either way, all Americans will suffer.

By Aaron Bernstein in New York, with bureau reports

Rex Rystull

REVENGE OF THE SMALL FRY

They're stoking stock funds despite the pros' pessimism–and they're looking pretty savv

Chalk one up for the little guy. While scores of Wall Street strategists were talking down the Dow, the small investor was jumping in with both feet. In just two months, December and January, investors poured an estimated $41.5 billion into stock mutual funds. That's on top of the $112 billion they plowed into the market in the first 11 months of 1995. And after racking up a 37% gain in 1995, the Dow has barreled ahead an additional 463 points in 1996, or about 9%. It's hard to find a market strategist whose yearend stock-market forecast wasn't blown out of the water in just the first six weeks of 1996.

Indeed, as the small investor was throwing money into stock mutual funds, many fund managers were retreating into cash. Case in point: Jeffrey Vinik's $56.7 billion Fidelity Magellan Fund. As of Dec. 31, 1995, the fund had 32.1% of its assets in cash and bonds, mainly in Treasury securities—vs. 4.3% at the end of October. As Vinik was accumulating some $14 billion in cash between October and December of 1995, the Standard & Poor's 500-stock index rose 13.5%. Little wonder that so far this year, Magellan is up 3.3%, compared with about 7% for the S&P 500.

DRIVING FORCE. Will small investors enjoy a year of solid returns in 1996? Or will that old saw about the small investor moving into a bull market late in the game prevail? As the Dow scales new heights, strategists are becoming more jittery, warning investors to keep to the sidelines. To be sure, markets don't move in a straight upward line. They do correct. But the forces propelling this market to record highs are still in place—and some are gaining momentum. Much of the power behind this market comes from low interest rates that are expected to go lower, inflation that is almost nonexistent, and earnings growth—in real terms—that is robust. "The fact that stocks are up so sharply does not mean that the market is wrong," says Alfred Goldman, an analyst at A. G. Edwards & Sons Inc. "It means that we analysts underestimated the power of its underlying momentum."

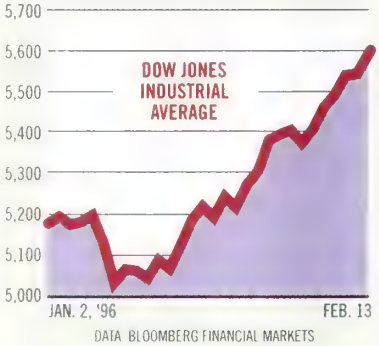
A new element has been added to the momentum of this market: As companies shift away from defined-benefit pension plans and put employees into self-directed 401(k) plans, individuals are being forced to take more responsibility for the investment decisions in their retirement plans—and are increasingly choosing stocks and stock funds. Indeed, more and more of them are going into stock-index funds, which, unlike Vinik's Magellan Fund, stay fully invested in the market.

To David Shulman of Salomon Brothers Inc., winning the war on inflation means that the old ways of judging whether a stock, or the overall stock market, is fairly valued have to be tossed out the window. "Instead of valuing stocks at multiples ranging between 12 to 16 times trend earnings [normalized historical earnings going back to 1960], a multiple of 16 to 20 times trend earnings might be more appropriate, which is where stocks traded in the 1960s," argues Shulman. Right now, the market is selling at a 17.7 price-to-earnings multiple, and with many companies reporting higher-than-expected earnings, it could actually be undervalued rather than overvalued.

Don R. Hays of Wheat First Butcher Singer in Richmond, Va., agrees that the stock market is undervalued and thinks that its stellar performance—outperforming every major world stock market (table)—will continue. "Investors are now going to benefit from corporate downsizing, government cutbacks, and the discipline of eliminating the threat of inflation from the economy," he says. Ha envisions an era where a Dow at 5600 "the beginning of the stock marke best 15 years for the small investor."

Even some of the old ways of valui stocks suggest that the bull has roo to run. Looking at data from 1978 1993, Stanley Levine, director of quan tative research for First Call Corp., us the relationship between the price-ear ings multiple of the S&P 500 and the yie on the 10-year U.S. Treasury bond calculate a fair value for the stock ma ket. For example, when the 10-ye Treasury yields 7%, a fair value for t p-e multiple on the S&P 500 would te to be around 14. When the bond yiel

THE DOW TAKES OFF...



DATA: BLOOMBERG FINANCIAL MARKETS

...OUTPACING THE WORLD'S BOURSES

	ONE-YEAR GAIN* (PERCENT, IN U.S. DOLLARS)
U.S. (DJIA)	41.4%
CANADA (TSE 300)	25.0
BRITAIN (FT-SE 100)	20.3
GERMANY (DAX)	16.8
FRANCE (CAC 40)	9.5
JAPAN (NIKKEI 225)	6.5

*year ending Feb. 13 DATA: BLOOMBERG FINANCIAL MARKETS

TIMBER?

Strategists are getting more anxious every day–yet the forces behind the market's highs are still in place

, the p-e multiple would be around a ½ target. Right now, with the 10-year nd at 5.6%, and factoring in the 12-nth forward earnings forecasts for the P 500, the historical relationship sug-sts a value of 767 for the S&P 500, a % jump from its current level of 660. Falling interest rates are a tonic for e market for another reason: Liquid sets, such as certificates of deposit d money-market funds, become less tractive relative to stocks. "Short rates are coming down and there is no prospect of their improvement, so money has to go into stocks to get a decent return," says John H. Shaughnessy, a strategist for Hartford's Advest Group. Edward G. Riley, chief investment officer of the Private Bank at Bank of Boston, says there is a pot of about $300 billion in small CDs and money-market funds that may find its way into stocks if short-term rates go lower.

As in any bull market worth its salt, there are loads of concerns about too much speculation. First Albany Corp. market strategist Hugh A. Johnson is concerned that margin debt had risen to 1.3% of the value of shares listed on the New York Stock Exchange as of the end of December. Typically, margin debt makes up less than 1% of the value, he says.

Elaine M. Garzarelli of Garzarelli Capital, who is forecasting a 6500 Dow by yearend, is more concerned about the rising level of bullish sentiment, which historically has signaled a market top. The sentiment indicator in her model, however, is still neutral. The same situation prevails at *Investors Intelligence* newsletter. The advisers polled by the newsletter are at their most bullish since January, 1992—with 53.8% bulls and 29.4% bears. Nevertheless, *Investors'* technical model remains bullish on the market.

DECENT GROWTH. One of the biggest worries among strategists is that the economy will respond too quickly to easing monetary policy. "If economic activity moved from its current 2% up to 3% or 3.5% in the second half of the year, then the Fed would stop easing, long rates would firm, and that could stanch the flow of money into mutual funds," says Shaughnessy. But market watchers say that's a long shot, pointing to the sluggishness in retail sales and wage growth. First Call's Levine notes that Wall Street's big guns, the investment strategists, are forecasting just 5% growth in operating earnings in 1996. The broader universe of stock analysts, however, while cutting their estimates in recent weeks, are still looking for decent growth of 12% in operating earnings.

If there is a major correction looming, strategists have a hard time envisioning what could spark it. "Unless the market moves substantially above 6000, the risk is not substantial," says Dean Witter Reynolds Inc. strategist William Dodge. "This market now has the wind at its back like it wants to get overvalued, so that may be in store, but it's too early." Bank of Boston's Riley notes that since World War II major corrections have typically been associated with a major rise in interest rates of 125 basis points or so—a scenario that seems highly unlikely today.

With many strategists still fighting the tape, 1996 may be the second year in a row when small investors look a lot more savvy than the professional market mavens. A. G. Edward's bullish analyst, Alfred Goldman, offers this advice to his fellow strategists: "Traders should be ready to quickly buy pullbacks. Bears should reorder their ulcer medication."

By Suzanne Woolley in New York

PHILIP ANDERSON

BLANCHARD: *He says he may lay off as many as half of Deluxe's officers*

TECHNOLOGY

DELUXE ISN'T CHECKING OUT YET

The check processor finally is focusing on electronic services

For nearly a decade, Deluxe Corp. has been trying to cope with the inexorable atrophy of its core product: the check.

The St. Paul (Minn.) company has been printing and processing checks for its entire 81 years and dominates the industry with more than a 50% share. Drawing on the rich cash stream of its check business, it has spent a staggering $650 million diversifying into everything from electronic-payment technology to greeting cards. And what does Deluxe have to show for its effort? A collection of new businesses that contributes nearly half of the company's revenue but less than 10% of its profits.

In 1995, earnings fell for the third straight year, dragging the company's share price down. Margins are under severe pressure as the bank merger wave produces bigger institutions that are forcing down check prices. Deluxe is also facing stiff challenges from 30-odd competitors in marketing checks directly to consumers. And it is losing ground to the regional electronic funds transfer (EFT) networks and to First Data, Electronic Data Systems, and MCI Communications, which are staking out positions in new electronic-banking businesses.

Faced with these difficulties, Deluxe is now being turned upside-down by a new CEO, John A. "Gus" Blanchard III, the first Deluxe chief not steeped in company tradition. His challenge is to protect what's still Deluxe's largest business, while investing more astutely than his predecessors in new electronic ventures. In recent weeks, Blanchard has launched a furious cost-cutting and restructuring program designed to better focus the company's efforts on developing and selling a variety of promising transaction services—check verification, home banking, ATM switching, and EFT settlement—for banks and EFT networks, its core customers. Deluxe, Blanchard says, "has a set of tools that can be of enormous use to financial institutions" as they shift from checks to electronic payments.

In late December, Blanchard began unveiling moves he hopes will cut $1[illegible] million in costs by the end of 1997. He has announced plans to close 26 of [illegible] check-printing plants, cut capital spending by 30%, and shed Deluxe's ink-manufacturing and financial-forms businesses. He has reorganized operating units for the first time bringing electronic businesses under the same management as checks. He's studying whether Deluxe should keep selling greeting cards and stay in the low-margin business of electronically processing welfare and food-stamp benefits. And he says he is likely to lay off 30% to 50% of the company's officers. "Everything seemed disconnected," says Blanchard. "There's a great opportunity for focus."

PROMISING A REBOUND. Prompted by Deluxe's dismal performance, the Deluxe board recruited the 53-year-old Blanchard last May to replace Harold V. Haverty, who was approaching retirement age. Analysts and rivals think he has what it takes to turn the $1.8 billion company around. He's promising investors an earnings rebound this year. "He has got the organization on track," says Rudolf A. Hokanson of Deutsche Morgan Grenfell, a London investment bank.

A longtime AT&T sales and marketing executive, Blanchard appears to understand how to manage companies buffeted by technological changes. Most recently, he earned accolades as executive vice-president at General Instrument Corp., where he helped the maker of cable and interactive technologies maneuver into new foreign markets. Indeed, Blanchard will need to tap every bit of ingenuity he can muster to position Deluxe in the highly competitive financial transaction services market.

Rivals and customers suggest that Deluxe's questionable diversification strategy took its attention away from important trends in technology and pricing. One example: A key Deluxe business, selling processing services and software to regional networks of ATM operators, is now being squeezed because some of the biggest networks are processing transactions in-house. "They were simply not aggre-

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sive in product development and pricing," says Richard P. Yanak, president of NYCE Corp., the No. 2 network, which now does its own processing.

Blanchard also discovered that Deluxe's check and electronic units were sometimes competing with each other for the same customers. "You have a feeling that the left hand sometimes doesn't know what the right hand is doing," says a senior bank executive whose institution is a Deluxe customer.

Blanchard realizes that Deluxe must work with banks, not compete with them. In moving into home banking, he plans to position Deluxe as an intermediary between banks and big software providers like Microsoft Corp. and Intuit Inc. by providing processing and customer database information. He's now prospecting for investment opportunities to bolster a fledgling home banking software company Deluxe bought in 1994.

Aiding this push is the reservoir of goodwill Deluxe enjoys among many bankers. Keith K. Theisen, a vice-president at Norwest Corp., also sees a new responsiveness to customers: He recently received his first call from Deluxe's chief technology officer. "This shows they must have awakened to the need to deal with their clients' issues," says Theisen.

Blanchard even seems to be getting his own managers from different units to work together. One result: On Feb. 12, the company announced a new product that enables banks to screen out bad customers by linking Deluxe's check-ordering database with its check-approval software. Now, if he can only infuse the whole company with that sense of focus, Deluxe could avoid going the way of the check.

By Richard A. Melcher in St. Paul, Minn.

DELUXE REDUX?

THE OVERHAUL PLAN

COST-CUTTING Save $150 million by closing 26 of 41 check plants, nearly halve executive posts, exit peripheral businesses

RECONFIGURING Rethink such non-core units as greeting cards and electronic delivery of food stamps

EXPANSION Acquire companies in electronic financial processing for banks and ATM networks, roll out new home-banking switching programs, boost international sales

A COMPANY [illegible]

MARKETS

GO FORTH TO THE U.S. AND PROSPER

Israeli high-tech startups find a warm reception on NASDAQ

America's tech-stock fever has reached Israeli shores. But the hottest action isn't in Tel Aviv. It's on America's NASDAQ stock market.

With local entrepreneurs long counting on Wall Street investors to snap up the best of Israel's high-technology equity offerings, investment banks are now lining up as many as 30 new issues to go public on NASDAQ in 1996, predicts Shlomo Kalish, managing director of Jerusalem Global Consultants. All told, Israelis may unload a record $700 million to $800 million in new shares and secondary offerings this year, up from $450 million in 1995.

Enthusiasm is so high that shares in one hot company that went public in February—ESC Medical Systems Ltd., a maker of devices to zap varicose veins with pulses of light—nearly doubled in value in their first few days of trading on NASDAQ. The company, whose 1995 sales and earnings were $8.4 million and $2.8 million, respectively, now trades at $25, with a price-earnings ratio of 55.

WHY NOT? In listing its stock in the U.S., ESC joined 65 other Israeli high-tech companies already trading on Wall Street, including equipment maker ECI Telecommunications, whose shares climbed 88% last year, and Teva Pharmaceutical Industries, up 77%. Now, investors are salivating over what's likely to come next.

And why not? Israel's booming economy, the peace process, and the Arab boycott's end are buoying hopes. Among NASDAQ initial public offerings expected soon: CheckPoint, a leader in network-security software, and Orbot Instruments, a maker of semiconductor inspection devices. Tadiran Telecommunications, a maker of telecom and networking equipment, also is expected to sell stock. Adding to the IPO frenzy is the arrival of a clutch of tech-oriented American investment banks including Robertson Stephens, Cowen & Co., and Montgomery Securities. "The entry of the highly specialized technology boutiques is a further upgrading of Israel on the international investment map," says Ron Lubash, a managing director at Lehman Brothers Inc. in Tel Aviv.

The new firms' arrival in the Israeli market is producing cutthroat competition for deals and fears that bankers are lowering their standards, says Zeev Holtzman, managing director of Giza Ltd., a Tel Aviv consulting firm. Holtzman fears that some companies not yet ready for the market are going public. His concerns recall a similar epidemic of tech-stock mania that swept Israel in the early 1990s. That one resulted in the failure of a number of offerings. But many traders think this public offering movement is on firmer footing. As long as Israel continues producing more than its share of high-tech winners, the investment bankers will be on the prowl for the next generation of success stories.

By Neal Sandler in Jerusalem

A Rush to Sell New Shares

Israeli initial public offerings in the U.S.

COMPANY	SALES/MILLIONS
VOCALTEC Produces software for making phone calls on the Internet. Raised $7.5 million in February.	$2
ESC MEDICAL SYSTEMS Makes devices to treat varicose veins. Raised $46.5 million in February.	8
...and ones on the way	
TADIRAN TELECOMMUNICATIONS Makes telecom equipment. Wants to raise $90 million to $110 million.	400
CHECKPOINT Makes network-security software. Plans to raise an estimated $40 million.	16
ORBOT INSTRUMENTS Makes semiconductor inspection gear. Hopes to raise $15 million to $25 million.	34

DATA BUSINESS WEEK

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MONEY MANAGEMENT

ARIEL'S FALL FROM GRACE

John Rogers is trying to revive his sagging investment firm

For seven years, John W. Rogers Jr. enjoyed strong ties to Connecticut's Treasury Dept. His firm, Ariel Capital Management Inc., managed $82.9 million in pension funds for the state. But last March, when Rogers showed up for an appointment with Christopher Burnham, the new state treasurer, he was fobbed off on a couple of aides. Rogers never did meet with Burnham, and on Aug. 29, Burnham fired him.

Once hailed as one of the nation's hottest money managers, Rogers, 37, is beginning to look like an also-ran. The soft-spoken Princeton grad who at 23 launched what is today the country's largest minority-owned money-management firm, has fallen out of favor. As several big investors pulled out over the last 18 months, assets under management have slid from $2.1 billion in 1994 to $1.6 billion.

TOUGH TIMES: *Rogers partly blames a new political tide*

Rogers earned his reputation as a hot stock-picker in the 1980s. He even weathered the 1987 market crash and earned double-digit returns that year. But his hand has gone cold in the 1990s. His strategy of pursuing stocks in out-of-favor sectors such as manufacturing and consumer products at a time when technology and health care have dominated the market hasn't helped. For the five years ending Dec. 31, the Ariel Growth Fund, a mutual fund launched in 1986 that serves as the firm's flagship, earned an average annual total return of 12.9%, vs. 17.1% for the average small-cap value fund, according to Morningstar Inc. Says Rogers: "This has been the toughest time of my life."

CONSERVATIVE ROADBLOCKS. Some of his troubles, though, can be blamed on the changing political climate. During the late 1980s and early 1990s, minority firms were welcomed by many state and local governments to manage pension funds and other assets. But as the conservative tide rises, firms such as Ariel are getting less benefit of the doubt. Says pension consultant Budge Collins: "There is less favoritism to minorities than there was in the past. We're all more performance-oriented."

The Connecticut episode is a case in point. Under the state's three previous treasurers, all of whom were African American, Rogers says he had no problems. But when Republicans swept into office in 1994, Rogers says, the sta began closing its doors to minorit owned firms. "Dealing with minori firms is not important" to Burnha Rogers claims. "We were just a minori firm that the black treasurer had hire

Burnham insists that performance not politics—prompted Ariel's firin While Ariel had an "excellent perfo mance" at first, Burnham says that t firm failed to beat the Russell 200 index—a benchmark for small-ca stocks—in recent years. Eve more, he says, political favor ism has long plagued Connec cut's pension fund, and inves ment returns suffered. Burnha cited campaign records showin Rogers personally gave $1,0 to the 1994 election committe of former Treasurer Joe Sugg who was defeated by Burnha

WEALTHY BLACKS. Rogers sa the conservative sweep co him a Los Angeles city accou as well after the 1994 election But he concedes that he al lost business with Detroi which went from one bla mayor to another.

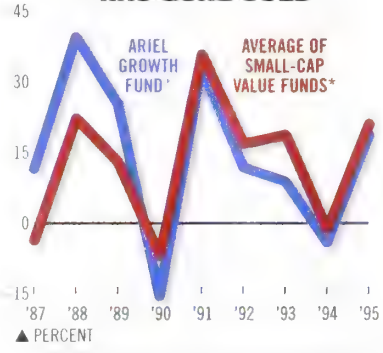
Rogers is now scramblin for new clients. His plan i volves marketing three mutu funds managed by Ariel to largely overlooked marke middle-class and wealthy Afr can American families. "Blac are perceived to be consumers and n savers and investors," says Mello Hobson, Ariel's marketing director. B she adds that African Americans' i comes are rising to the point whe more of them are investing the money.

Rogers is courting those investors b advertising in such publications as *Bla Enterprise* and lobbying black-owne businesses to include Ariel funds in the 401(k) plans. In a move to help divers fy the firm's offerings, Rogers launche a bond fund and hired an outside firm t manage it.

Rogers hopes this action will allo Ariel to reclaim its glory. "We've lost lot of good, long-term clients," he l ments, "and it's disappointing whe people you thought had faith and conf dence in you call and say, 'We're goin to someone else.'" Despite the exodu Rogers says, he plans no changes i his investment strategy. But if his col hand doesn't warm up pretty soo he'll discover that black investors, lik white ones, are ultimately loyal to th color green.

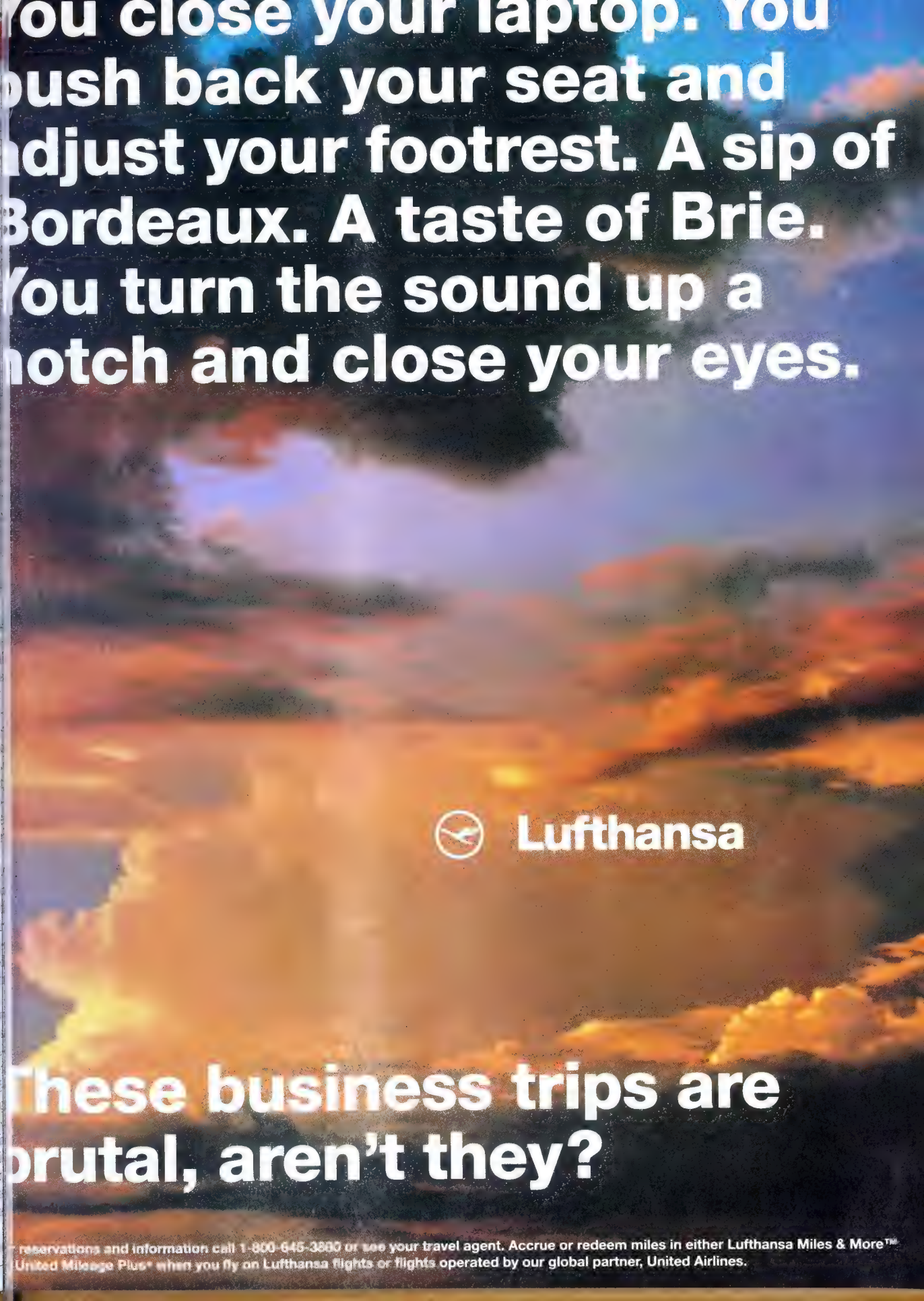
By Ron Stodghill II in Chicag

ARIEL'S HOT HAND HAS GONE COLD



*PRETAX TOTAL RETURN, INCLUDES APPRECIATION AND REINVESTMENT OF CAPITAL GAINS AND DIVIDENDS

DATA: MORNINGSTAR INC.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BY GENE G. MARCIAL

THE CHEMISTRY AT EASTMAN CHEMICAL

Merger mania has yet to hit the chemical industry in a big way. But that may change, say some buyout investors who have been loading up on Eastman Chemical (EMN), a worldwide producer of plastics, chemicals, and fiber products. These pros are betting on whispers that Dow Chemical (DOW) and Germany's Hoechst are in the market for an acquisition—and Eastman Chemical is the prey.

Eastman's stock doesn't yet look like

DATA BLOOMBERG FINANCIAL MARKETS, NELSON PUBLICATIONS

the company is in anyone's gunsight. At 68, the Big Board stock is a shade below its September, 1995, high. So far this year it's up about 6 per share, or 9%, keping up with the market. One analyst values Eastman at 90 to 100 a share in a takeover, based on solid earnings and a broad portfolio of products. Formerly a division of Eastman Kodak (EK), the company, headquartered in Kingsport, Tenn., was spun off to shareholders on Dec. 31, 1993, as the photo giant tried to rid itself of businesses unrelated to photography and imaging.

One investment manager who has been accumulating Eastman shares sees a "very natural strategic fit between Eastman and the rumored suitors." Dow Chemical, the nation's second-largest chemical company, produces basic chemicals as well as plastics and household, drug, and agricultural products. Dow, which continues to be plagued by lawsuits over silicone breast implants manufactured by its 50%-owned Dow Corning unit, is looking for new growth through acquisitions in its core business. "Eastman Chemical is one of the companies Dow is looking at," adds this money manager.

Hoechst is pretty much in the same lines—chemicals, agricultural products, and pharmaceuticals, and it has acquisition experience: In the mid-1980s, it acquired Celanese. The $8 billion or so it would take to acquire Eastman would not be a problem for either of the deep-pocketed giants.

This manager thinks even at 90 to 100 a share, Eastman isn't expensive considering its strong earnings growth plus "management's effective and productive performance." He doesn't believe Eastman is looking for a buyer but that an offer of 90 to 100 may prove irresistible. In 1995, the company earned $559 million on $5 billion in revenues, or $6.78 per share, a 67% per-share gain over 1994. So far, 1996 earnings forecasts are not much higher than 1995's. But in 1997, analysts figure, earnings should show a neat rise (chart). Spokesmen for Eastman and Dow Chemical declined comment.

A HOT PLAY IN...STEEL?

Universal Stainless & Alloy Products (USAP), which went public in late 1994 at 8¼, was not one of those initial public offerings that doubled its first day. But this is stainless steel, not the Internet. Still, the stock gained some ground and reached 15 in July—then near-disaster struck. A steel-rolling machine malfunctioned at the company's Bridgeville (Penn.) minimill, shutting down operations for five weeks.

That episode might have doomed many other small companies. But under President and CEO Clarence "Mac" McAninch, Universal recouped quickly and went on to report a 56¢ per-share profit for all of 1995 vs. a loss of 62¢ a share in 1994. For the new year, Scott Kalb, managing director at Smith Barney International Asset Management, sees an even brighter picture: earnings of $1.60 a share. If he's right, the stock is a screaming buy, selling for a scant 8 times this year's earnings. For 1997, Kalb forecasts a huge $2.10 to $2.20 a share. So Kalb sees the stock at 12¼, reaching as high as 20 over the next year.

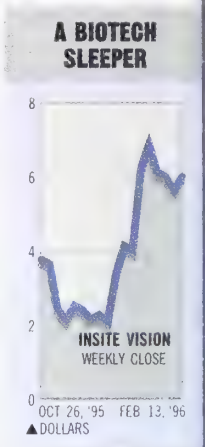
Analyst Harris Cohen of Furman Selz, one of the IPO's underwriters, says management continues to build a solid customer base with its niche products. Universal produces only semi-finished stainless steel. He was impressed tha during the fourth quarter, Universa signed up new customers accountin for about $11 million in annualized rev enues. For a company with 1995 reve nues of $48 million, that's a significan gain.

INSITE'S CLEAR VISION

At first glance, InSite Vision (INSV looks like a major flop for Morga Stanley (MS), which brought the compa ny public in October, 1993, at 11 share. The stock has gone south since hitting a low of 1½ on Nov. 3, 199 But in mid-December, it started t head north, reaching 7½ by mid-Janu ary on heavy trading. That's when th company, which is developing pharma ceuticals to treat glaucoma, announce positive data on clinical trials for two o its products.

The stock is now at 5¹³⁄₁₆, but fan think the best is yet to come. "Th company is one of the big sleepers i biotech, and we have raised our two year target for the stock to 30 share," says Michael Murphy, editor o the *California Technology Stock Letter*

Murphy thinks InSite will take step toward that target in the next few months for two reasons: He expects the company will file a patent application for a gene it has identified that produces a protein linked to glaucoma. This gene appears to protect cells and may arrest the development of glaucoma.



DATA BLOOMBERG FINANCIAL MARKETS

Murphy says the patent will also cover a genetically based diagnostic test for the illness He expects the company will link up with a strategic partner, perhaps Pharmacia & Upjohn, to market the diagnostic product and develop the gene into a viable treatment. Murphy says InSite and Upjohn were in serious negotiations for such a partnership before, but the talks were tabled when Upjohn received the merger offer from Pharmacia. "This is a huge deal," says Murphy.

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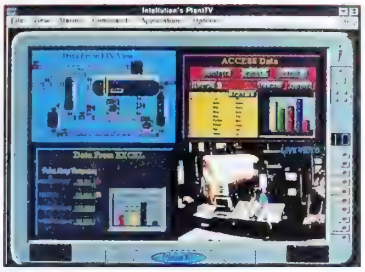

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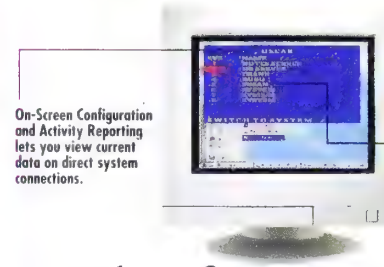

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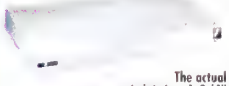

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Technology Guide Issue Date	Business Week Editorial Report Issue
June 24	Annual Report on Information Technology
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IDIDATES

OR STEVE, THEY ISS AND MAKE UP

arreling supply siders unite behind his Presidential bid

When Bear Stearns Chairman Alan "Ace" Greenberg threw a fund-raising dinner for GOP Presidential candidate Steve es at the Waldorf-Astoria Hotel December, the guest list read like a s who of supply-side economics. No rise there: Forbes is running as the er of the Reaganite flame of tax sound money, and optimism. More king was the fact that the ly side's warring clans set e their feuds to gather on es's behalf. "Wanniski and er in the same room—that's ething I haven't seen in s," says Cato Institute econ- st Stephen Moore. "They stand each oth- ut they're rally- behind Forbes." That's pulling sup- siders together is ared hope of see- a disciple in the te House. For 20 's, as a reporter editor-in-chief of family-owned magazine, es diligently studied tax-cut- gospel and libertarian social d with such apostles as writ- ude T. Wanniski and econo- Arthur B. Laffer. Although 17% flat-tax proposal lost m in Iowa, Forbes hopes to e at the top of the GOP pack ax-phobic New Hampshire's . 20 primary.

OT OF INK. So far, Forbes been running on the intellec- capital he has accumulated. as his Presidential campaign ures, the consultants and nomists who tutored him are ning an economic brain trust broaden his agenda beyond flat tax, a return to the gold ndard, and disdain for balanc- the budget.

Of all Forbes's advisers, Wan- i has gotten the most ink. A former editorial writer for *The Wall Street Journal*, Wanniski now runs Polyconomics Inc., a Morristown (N.J.) company that monitors political and economic trends for money managers. "Steve has a cast of characters he looks to for primary, fundamental advice on public policy, and I'm one of those characters," he says. Wanniski pushed Forbes to enter the race after former supply-side hero Jack Kemp announced in early 1995 that he would pass up a Presidential bid.

Most supply siders, dismissive of traditional economics, prefer to describe themselves as "political economists." Wanniski, who has no formal economic training, even claims that Lyndon H. LaRouche Jr., the four-time Presidential candidate who was convicted of mail fraud in 1988, is a member of the supply-side camp. LaRouche—who charged that Queen Elizabeth II heads a worldwide drug-trafficking network and that Henry Kissinger was a Soviet agent—is "a gold-standard guy," Wanniski explains. His firm has hired several of LaRouche's followers because "they're not trained in demand-model economics." Little wonder that some Forbes aides try to disown Wanniski: "Jude is full of ideas, and about one in five is worth listening to," sniffs one adviser.

Another member of the Forbes brain trust, though less visible, is Lawrence Kudlow, a Reagan Administration budget official and Forbes chum. Kudlow and Forbes fashioned the tax-cut platform that carried Republican Christine Todd Whitman to an upset victory in the 1993 New Jersey gubernatorial race. Kudlow, who later lost his job as chief economist at Bear Stearns Cos., forged a close bond with Forbes last summer, when the publisher gave him emotional support during his treatment for cocaine addiction.

Kudlow now works for Laffer's La Jolla (Calif.) consulting firm. He cautioned Forbes last spring about the media scrutiny and pressure that a campaign would bring to bear on his family and business interests. While Forbes was deliberating, he and Kudlow visited GOP Presidential candidate Senator Phil Gramm (R.-Tex.) in his Senate office to see if the Texan would carry the flat-tax banner. Friends of Forbes say that Gramm's lengthy monologue, which gave

Forbes's Economic Brain Trust

▼ GRACE-MARIE ARNETT Recently joined the Forbes campaign as policy director. A health-care consultant, she served as staff director for the GOP's Kemp Commission on tax reform.

LAWRENCE KUDLOW Former Reagan Administration OMB official and Bear Stearns economist. He worked with Forbes on the campaign of Governor Christine Todd Whitman (R-N.J.). Now a consultant with Laffer, Canto & Associates.

ARTHUR LAFFER ▶ Famous for inventing supply side's "Laffer Curve," which predicts higher tax revenues from lower tax rates. Runs his economic consulting firm in La Jolla, Calif.

ALAN REYNOLDS Former associate of supply-side advocate Jude Wanniski, Reynolds is now with the Hudson Institute. He served as Kemp Commission research director. Trying to line up academic economists to support the flat tax.

▼ JUDE WANNISKI Former *Wall Street Journal* editorialist and tax-cut booster. He helped persuade Forbes to run for President. Head of Polyconomics Inc., a political and economic consulting firm in New Jersey.

DATA: BUSINESS WEEK

CLOCKWISE FROM TOP: PHOTOGRAPHS BY STEVE ... SQUAMA-LA SOLLA; ROCKY THIER FOR BUSINESS WEEK

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only a curt nod to Forbes's concern convinced the publisher that he wou have to run if he wanted supply-si ideas to be aired. In January, Gram belatedly came out with his own 1 flat-tax plan and bashed Forbes's pr posal to eliminate mortgage-intere and charitable-gift deductions.

Forbes aides point to three oth steady sources of ideas. Laffer, the Ca fornia economist whose "Laffer Curv helped persuade Reagan in the ear 1980s that slashing tax rates would act ally lift tax revenues, advises Forbes taxes and the dollar. The campaign tur to Alan Reynolds, chief economist at t Hudson Institute, to field questions taxes. Reynolds served as research dire tor for the GOP's tax-reform commissio chaired by Kemp, which called for a g neric version of Forbes's 17% plan. Fla tax guru Alvin Rabushka of the Hoov Institution is another idea maven.

The job of coordinating Forbes's po icy stances falls to Grace-Marie Arnet who joined the campaign on Feb. 8 aft a stint as staff director of the Kem Commission. Arnett is a health-care co sultant who shares Forbes's enthusias for medical savings accounts, emplo er-sponsored funds that let worke keep any money they don't spend o basic medical bills. (Forbes set up MSA for his own employees in 1992.)

THE YACHT CLUB? The candidate's ow writings, laid out over the years in h Fact & Comment column in *Forbe* clearly put him in the camp of fring supply siders who believe that defici don't matter. That could be a public-rel tions problem if a strong showing in Ne Hampshire lifts the multimillionaire's ca didacy out of the novelty stage. Suppl siders "are not members in good stan ing of the economic fraternity," chuck les a Clinton Administration economist

GOP rivals are eager to seize o Forbes's unusual crew of brain-truste to paint him as an economic extremis willing to sell out the middle class. Se ate Majority Leader Bob Dole (R-Kan. the GOP front-runner, raises fears abou Forbes's scheme to partially privatiz Social Security, while neopopulist com mentator Patrick J. Buchanan accuse Forbes of drafting his flat tax "for th boys down at the yacht basin."

True, blue-sky economic optimis and faith in the healing power of ta cuts have taken a beating since th Gipper rode into the sunset. But Stev Forbes, with his open checkbook an gang of fellow true believers, is bet ting that the supply-side sequel ha box-office appeal in 1996.

By Mike McNamee in Washingto

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AUTOS

JAPAN TURNS A CORNER

Carmakers come on strong around the globe

Last spring, the mood at Nissan was dismal: Like all of Japan's auto makers, the company was suffering from a rising yen, falling sales, and a looming trade war with the U.S. Breaking a long-standing taboo, Nissan Motor Co. shuttered its Zama assembly plant near Tokyo. To cut payrolls, Nissan dropped the minimum age for "retirement" buyouts to 30, and some 1,600 employees took the offer. "We experienced heaven and hell in only three years," sighs Tadao Takei, a Nissan executive vice-president.

Now, however, Nissan is emerging from the depths. The yen has softened dramatically, and the Japanese economy is growing again. The auto trade war has faded away, and Nissan expects to show a profit this fiscal year, after three years in the red. "The recovery we expected in 1995 will actually happen in 1996," says a relaxed President Yoshifumi Tsuji. As usual, the superficial calm conceals the real feeling. Nissan executives, one analyst says, "are really excited" by their profit rebound.

READY, SET... All of Japan's auto industry, in fact, is set to surge back after the rough ride of the early '90s. From the years of pain and retrenchment, Toyota, Nissan, Mitsubishi Motors, and Honda are emerging as a globally competitive Big Four. Although survival mergers were widely predicted, not one of Japan's 11 vehicle manufacturers has gone bankrupt or been taken over. Instead, the second-tier players are hanging on by allying themselves more deeply with bigger players or by focusing on narrower market segments. A still-troubled Mazda Motor Corp., for example, is narrowing its product range to survive, perhaps under Ford Motor Co.'s wing.

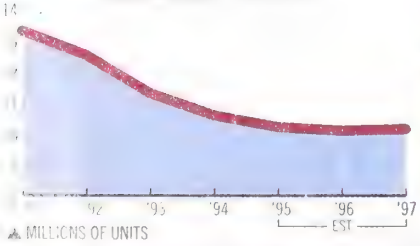
The winners will be impressive competitors. They've succeeded at cutting payroll fat through attrition and buyouts, leaving muscle largely untouched. New leaders and ideas have invigorated management's top ranks. Design is faster and more creative, and manufacturing is more efficient than ever. If the yen averages 105 to the dollar this year, that could double the industry's pretax income, to $8.5 billion. Revitalized profits will help the Japanese hold the line on prices worldwide and in some cases cut them.

New products with attractive pricing are at the core of Japan's strategy. In the U.S., the Japanese will push deeper into such longtime Detroit sanctuaries as minivans, sport-utility vehicles, and full-size pickup trucks. Toyota Motor Corp. is rolling out its RAV4 mini-sport-utility vehicle this month, starting at about $15,000, to compete with the Geo Tracker and Kia Sportage. A redesign of the popular Camry is expected to hit U.S. showrooms this f with a price cut of about $1,500 from t prior model's base of $17,000. Toyot full-size T100 pickup, priced arou $14,400, meanwhile, will issue from a n Indiana factory in 1998.

In luxury models, where sales ha been soft, Nissan will offer a more a gressively priced Infiniti Q45 later t year, grinding down development co by recycling its popular Cima model fr Japan. It will come in well below toda

How Japanese Auto Makers Have Transformed Their Global Positions

PRODUCTION IN JAPAN HAS FALLEN...



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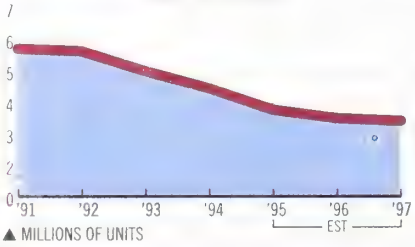

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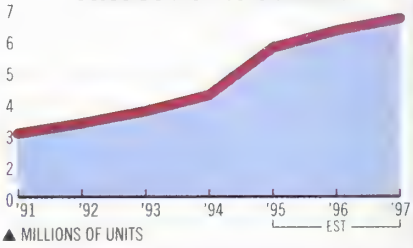

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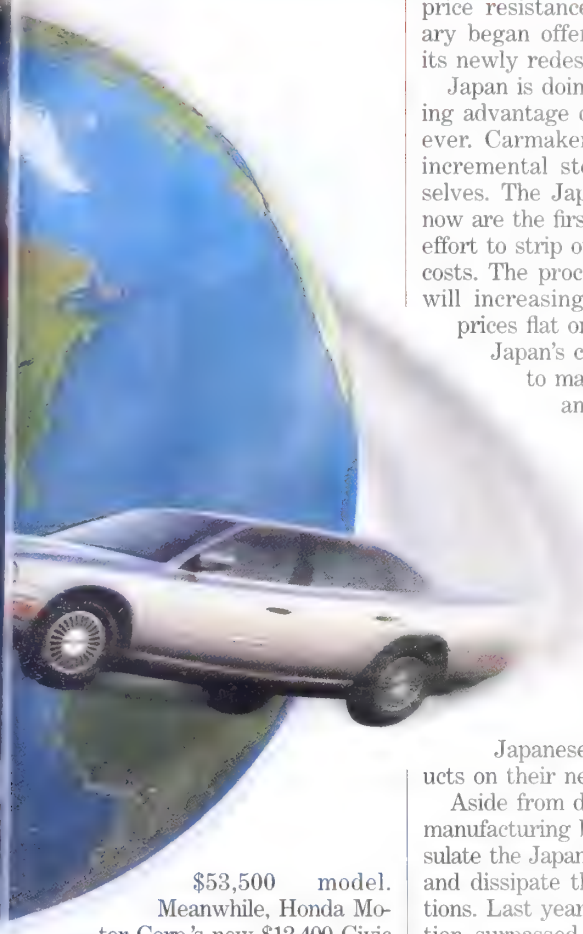
Note: All data for autos and commercial vehicles



$53,500 model. Meanwhile, Honda Motor Corp.'s new $12,400 Civic sedan, launched last fall with a 1% price increase, is already America's best-selling small car, ahead of General Motors Corp.'s Saturn and Ford's Escort.

The Japanese push is global in scale. Japan's carmakers are now multinationals, not simply exporters. The new cars increasingly are assembled in North America, Europe, and Asia and designed for local tastes. Mitsubishi has just begun assembling the Carisma sedan, with a price tag of about $20,000, in the Netherlands. In Asia, Toyota is tailoring more products specifically for emerging markets, such as its wildly successful Kijiang sport utility in Indonesia. Japanese makers have about 90% of the booming Southeast Asian market, a base that makes them more powerful globally.

LEAN AND MEAN. In short, Japan is set out to offer U.S. makers a new level of competition in all their important markets. Detroit has begun complaining that the yen's softening, from about 80 to the dollar to about 105—some 30%—is leveling the playing field. "We think it's hurting us because it gives the Japanese more opportunity to take more profits or reduce prices," said David N. McCammon, Ford's treasurer. Already facing price resistance, Ford in early February began offering cheaper versions of its newly redesigned Taurus.

Japan is doing more than merely taking advantage of currency swings, however. Carmakers have taken countless incremental steps to transform themselves. The Japanese models appearing now are the first to benefit from years of effort to strip out unnecessary parts and costs. The process, called "lean design," will increasingly allow Japan to hold prices flat or reduce them. Moreover, Japan's companies have continued to make strides in speeding up and improving their manufacturing cycles. "The Japanese have already shown signs of recovery, and it will escalate during the balance of the decade," figures Christopher W. Cedergren, senior vice-president at AutoPacific Inc. "We haven't seen the Japanese fully launch new products on their new lower-cost base."

Aside from driving down costs, global manufacturing bases increasingly will insulate the Japanese from currency swings and dissipate the threats of trade sanctions. Last year, Japan's offshore production surpassed exports for the first time (chart, page 108). If Toyota achieves its target of assembling in North America 92% of the vehicles it sells there, the threat of tariffs from Washington will ring hollow.

In this third wave of Japanese auto competition, there are important differences from the past. Unlike in the 1970s, when their fuel-efficient cars stormed in, or the 1980s, when they moved into larger cars, the Japanese are not reaching for big gains in market share. Now holding 22.9% of the mature U.S. market, the most bullish assessment at the moment is that Japan will gain a point or two in overall share, partly because of the new offerings in sport utilities, vans, and pickup trucks. "We're saying: 'Just keep our market share,'" comments Motoo Suzuki, executive vice-president at Mitsubishi Motors. "It's that kind of era." For now, Japan's emphasis will be on profitability.

The home market is also different than before. The days when Japanese consumers would pay anything for their cars are long gone. U.S. and European rivals are attacking the Japanese market, making modest gains. But a loosening grip on their domestic market is a price Japanese auto makers are willing to pay to mitigate trade friction, and the pain is softened by the fact that a quarter of last year's 380,000 imports by Tokyo came from Japanese plants abroad. Honda and Toyota have emerged as the largest exporters of North American cars, about half of which are headed for Japan. These "reverse imports" narrow trade deficits as measured by governments while allowing the manufacturers to continue expanding globally.

FUN FARE. Clearly, the Japanese carmakers will retain huge advantages in their home market. That's partly because they are ahead of foreign rivals in responding to newly finicky Japanese consumers, who now want unique niche models. Reflecting a boom in lifestyle products, consumers are demanding fun cars, such as Mazda's Bongo Friendee, which has a pop-up tent top for extra sleeping space on camping trips. Just as Americans changed years ago, Japanese customers have moved away from plain-vanilla sedans to "recreational vehicles," a category that in Japan includes station wagons, vans, and sport utilities. That began a wave of new designs.

Mitsubishi scored first with its Pajero sport utility in 1991. Some thought it a passing fad. Pajero and Toyota's Land Cruiser had been around for years without big sales. But today, recreational vehicles account for an incredible one-third of Japan's market, and all the makers have scrambled to redesign old models and design new ones. Toyota came out with a remodeled 4Runner, as well as the RAV4 and Previa minivan. Honda built the Odyssey minivan and the CR-V sport-utility vehicle.

None of these has yet produced a hit in the U.S., but they are helping hone Japanese marketing skills. Toyota is predicting sales of 40,000 to 80,000 of the RAV4. But it will be a test to see whether the small, underpowered vehicles meet U.S. tastes.

Honda's Odyssey is another experiment. In 1990, Honda set out to create a new "Chrysler-type" minivan from scratch. It brought Yasuaki Asaki from its Formula One race team in London

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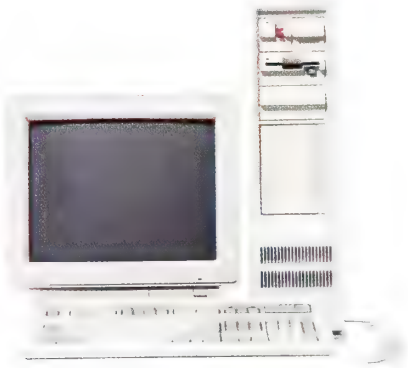

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back to Japan to design a 3-liter V-6 engine. But a year into development, the Japanese economy tanked, so Honda had to make do with the Accord's engine. Asaki fiddled to boost the horsepower from 135 to 145 and increase the torque. Although not as good as a newly designed engine, the switch allowed Honda to get its minivan in the showroom quickly—and at a lower development cost.

Overall, once Japanese engineers focused on costs, they quickly learned to improve performance while using cheaper, simpler parts that could be shared among models and fit into existing lines. The trick is cutting without completely "decontenting." Toyota execs learned a tough lesson when their remodeled 1995 Corolla bombed in Japan. Honda did better with its latest Civic, but some obvious features such as the cassette player and ashtray are gone nonetheless. "They're trying to reduce costs, but it's hard to squeeze blood from a turnip," says David Cole, director of the Office for the Study of Automotive Transportation at the University of Michigan. "The risk is that you cut back on the value the customer is looking for." The models rolling into world markets now seem to show a better balance between design and cost.

BROAD BASE. New management blood is also quickening Japan's comeback. The most notable example: Toyota's new president, Hiroshi Okuda, who was pulled from his post as vice-president for finance to energize Toyota's bureaucracy with his bolder, decisive style. "He has been making decisions quickly and set us really challenging targets," says Managing Director Fujio Cho.

Japan's companies also are starting to reshape middle management with incentives stressing merit. Honda, which has a large proportion of workers aged 45 to 55, is phasing in a new system over three years. Last year, roughly 15% of employees got higher-than-expected bonuses, and 15% got less. From 1997, managers at each level will have a fixed tenure, after which it's up, out, or down to part-time. None of these moves is revolutionary by U.S. standards, but the results will improve management over time.

Are U.S. auto makers ready for a new era of stiffer Japanese competition? In many senses, yes. For years, Big Three executives have been repeating the mantra: "Don't count the Japanese out." Detroit possesses heftier war chests than in previous battles, and Chrysler in particular has done well in stripping out costs. At a minimum, the breathing period these manufacturers have enjoyed because of the superyen is ending. That comes at a time of softness in sales and will clearly put pressure on profits.

The greater risk, however, is that Detroit hasn't quite grasped the incremental nature of what its Japanese rivals h achieved nor understood Japan's r global reach. Japan's Big Four will challenging from a much broader b this time, offering a complete family products. Deeply rooted in the U heartland with their manufactur operations, they also will be able to political protection in Washington. A they will be taking advantage of th ability to react more quickly to chang markets. Toyota, for example, driven down its development time to months for some models.

In a sense, the Japanese auto mak have come of age. The bold grabs market share that terrorized Detroi the past are giving way to a quest profits instead. Problems from too m manufacturing capacity at home and white-collar productivity will continue dog the Japanese. But with earnings the rise, they will have time and mo to solve those problems. As the Japan carmakers rev up around the world, t are securing their positions in the n round of the global auto shakeout.

By Edith Updike in Tokyo, with L ry Armstrong in Los Angeles, Kathl Kerwin and Keith Naughton in Det and David Woodruff in Bonn

GLOBAL PUSH

The Japanese are tailoring models f local markets. Th Carisma (left), by Mitsubishi, is aim at Europe; Toyota Kijiang sport utili at Indonesia

THIRD WAVE

In the mature U.S. market, where Honda's Accord is popular, Japanese carmakers are focusing on profits rather than market share

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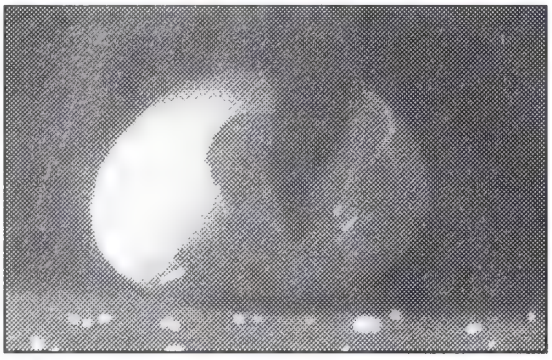

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MERICA'S NO. 1 CAR XPORTER IS...JAPAN?

ıt's right. The Japanese now outship Detroit

delegation of Chinese officials came to America last year in search of automobiles they could buy to help ıce China's growing trade surplus the U.S. Whom did they approach? urally, they went to Honda Motor and Toyota Motor Corp., America's two car exporters. "They wanted from our Ohio plant," recalls Yo uda, Honda's vice-president for ex- s from the U.S. Honda couldn't de- r, but Toyota was happy to oblige just began shipping Avalon sedans hina from its Kentucky factory.

While Detroit focuses on winning the le against Japan on U.S. soil, it's ng on the high seas. For the first e, the Japanese surpassed Detroit in th American car exports last year shipping 167,000 cars from U.S. and adian plants while the Big Three ex- ed 162,553. Detroit jumps way ahead, ı 316,000 vehicles, when trucks, mini- s, and sport utilities are counted, but an wasn't making those for export. w, as more Japanese trucks and mini- s roll out, many will be exported. e expect exports from North America increase steadily," promises Toyota sident Hiroshi Okuda.

A potent combination of high costs Japan and political expediency in the S. is pushing Japan's North American ansplants" into the exporting game. nda, America's No. 1 car exporter, otes 20% of its North American pro- tion to exports. Toyota, in four years, ns to more than double its American orts. That means it will be shipping re vehicles from U.S. ports than it eives from Japan, says Doug West, yota's U.S. group vice-president for ort and logistics.

LL SHELVES. Right now, more than f of Japan's North American exports urn to the Japanese market. Will se exports ease trade frictions? obably not anytime soon. So far, ey're making only a small dent in nerica's $60 billion-plus trade deficit th Japan. And the shipments don't solve the larger problem: U.S. auto akers continue to feel shunned by panese auto dealers. "We did not get into a trade negotiation [with Japan] to make sure the Japanese market would be open to Toyota and Honda," says Marjory E. Searing, deputy assistant secretary for Japan at the U.S. Commerce Dept.

Indeed, the Big Three managed to export a paltry 13,675 cars to Japan last year, although they had better luck with trucks, shipping out 23,450. Despite the trade agreement reached in June, U.S. executives charge that Japanese dealers still close their doors to Detroit. "This is all about shelf space, and we don't have good shelf space in Japan," says Andrew Card, president of the American Automobile Manufacturers Assn., the Big Three's Washington lobbying arm.

CRACKING KOREA. The Japanese argue their U.S. exports are just as important in resolving the trade imbalance as whatever Detroit can muster. But the Japanese fear their contribution won't count for much on Mar. 15, when Washington takes stock of how American companies are faring in Japan. "The Clinton Administration isn't focusing on the big picture. They're only looking at Detroit," said Philip Hutchinson, the Japanese auto makers' chief lobbyist in Washington.

Other countries on the receiving end of Japan's exports from the U.S. also aren't overly pleased. Ships loaded with U.S.-made Toyotas, Hondas, Nissans, Mazdas, Mitsubishis, Subarus, and Isuzus are arriving in Taiwan, a market that bars vehicles made in Japan for political and economic reasons. Another target is South Korea, which also is closed to vehicles assembled in Japan. Toyota, in particular, is launching a push into that market with its U.S.-made Avalons. Detroit is trying to crack the protected Korean market, too, but the transplants have an edge. "The kinds of cars Korea and Taiwan like are the ones that the Japanese make in the U.S.," says Linda Y.C. Lim, an Asian trade expert at the University of Michigan business school.

The Japanese reputation for knowing how to adapt their products for all markets sometimes leads to unusual requests from unusual markets. A Toyota distributor in Iceland just sent a letter to West to put in an early order for the T100 pickup trucks Toyota will begin building in Indiana in 1998. "It might not be a high-sales market," West says, "but I'm going to do everything I can to make sure he gets some trucks." It's that kind of thinking that is making the Japanese such formidable America-based exporters.

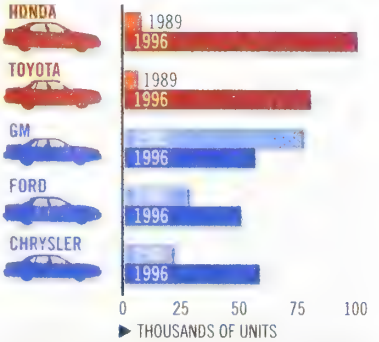
By Keith Naughton in Detroit, with Amy Borrus in Washington

STEERING EXPORTS

When officials from China visited the U.S. last year in search of cars, they called on Honda's Masuda first

THE JAPANESE GRAB THE LEAD

EXPORTS OF NORTH AMERICAN-ASSEMBLED AUTOS



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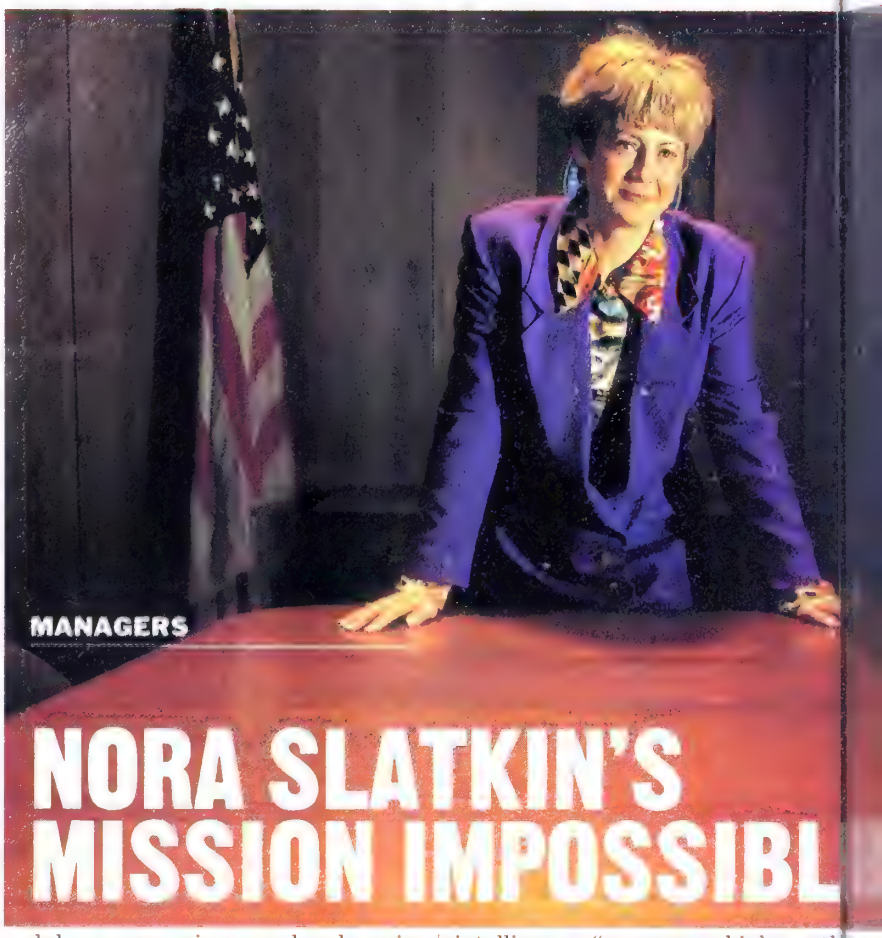


MANAGERS

NORA SLATKIN'S MISSION IMPOSSIBL

The CIA executive director must help rebuild morale and reinvent a furtive, balkanized bureaucracy

It was a Capitol Hill ritual in the late 1980s and early 1990s. When House and Senate conferees gathered to haggle over billions of dollars of weapons in annual defense bills, one aide from each side would stride to center stage and take charge. A bear of a man—6-foot, 4-inch, 235-pound John J. Hamre—would rise from behind the senators seated at the conference table. From the House staff seats would come his counterpart, a foot shorter and half his weight: data-devouring, Diet Coke-swilling, workaholic Nora R. Slatkin.

The physical mismatch was striking, but it didn't affect the legislative jousting. Armed with facts, figures, and moxie, Slatkin never wavered—and she won her share of bouts. Recalls an ex-Hill aide: "She was going to get clobbered if she didn't have a steel backbone."

These days, Slatkin needs those metal vertebrae more than ever. Last May, Central Intelligence Agency Director John M. Deutch named her to one of the toughest management jobs in America: executive director of the CIA. With Deutch focusing on relations with the President and Congress, Slatkin, 40, is not only the highest-ranking woman in CIA history but also the most powerful executive director in memory. Her job: running the day-to-day operations of a $3 billion agency that employs 17,000 people. Her mission: reinventing a bureaucracy stubbornly resistant to the accountability Congress is demanding. At the CIA, sighs former Director Robert M. Gates, "they understand how foreign policy and politics are carried out in every country in the world except one. Unfortunately, that's the one they operate in."

NOTORIOUS. Since May, Slatkin has been revamping the personnel system, disciplining wayward spooks, and trying to rebuild morale in the wake of the notorious Aldrich H. Ames case. But the CIA's furtive culture and dispersed workforce make it "an immensely difficult place to run," says an intelligence expert. "There's not any management school in the world that can prepare you."

To her critics, Slatkin's lack of cloak-and-dagger experience makes her singularly unprepared. "She wouldn't know an agent if he came up and kissed her," sniffs a former CIA officer. Slatkin's response is typically assured. "I have never met an agent in a backstreet of Lisbon," she concedes. "It doesn't mean I can't do this job." Operations chief David Cohen notes that Slatkin's job is not to run covert operations but to ask probing questions about their rationale—and "she's great at that."

In any case, being a woman may be a bigger problem than not being a spy. The CIA "is a time warp" when it comes to sexism, says one former government official. Last year, the agency settled a class action alleging sex discrimination, and the year before, a suit by a female former station chief who claimed male subordinates had concocted charges of alcoholism and sexual misconduct that ruined her career. (The station chief, Janine Brookner, had recommended disciplining Ames years before.)

Deutch says Slatkin's appointment carries an important message: Women in intelligence "can go as high as th abilities take them." But ex-CIA har who claim their feelings are shared dozens of current spymasters, dism Slatkin as "a demanding little blon from Brooklyn." (She actually was b and raised on Long Island.)

EXPLOSIVE REPORT. Undeterred, Slat has plunged into her job. One of first duties was to chair a panel viewing an explosive Inspector Gener report that charged two dozen ope tives with failing to reveal the links tween a Guatemalan colonel on the payroll and the murders of an Ameri innkeeper and a rebel married to American. The review was exhausti in part because she used it to le about reporting duties up the chain command and how case officers abr work. "She just kept pounding until did understand it," says Deputy Dir tor for Intelligence John C. Gann Slatkin, Gannon notes, likes to "h one more meeting than anyone want

Once the panel decided to sanct half of those implicated, Slatkin dic

"I have never met an agent in a backstreet of Lisbo

NORA R. SLATKIN

TITLE
Executive Director, Central Intelligence Agency

BORN
May 5, 1955, Glen Cove, N.Y.

EDUCATION
MS in foreign service, Georgetown University, 1979

BA in international relations, Lehigh University, 1977

CAREER
1979 Joined the Congressional Budget Office as defense analyst

1984 Moved to the House Armed Services Committee, where she was lead staffer on the procurement and military nuclear systems subcommittees

1993 Joined the Pentagon as special assistant to acquisitions czar John M. Deutch. Became an Assistant Navy Secretary, overseeing a $26 billion procurement budget

1995 Moved with Deutch to the CIA

EL KBONE: *hasn't d from iplining ward oks*

shy from the toughest task. She personally called the operatives to tell them of the penalties, which included several forced retirements. The sanctions spooked some spooks, who felt 1995 dis-

ıre standards were being applied to ɔns that occurred years earlier.

he daughter of an accountant and an e manager, Slatkin wanted to work the government since her days as of the first women at Lehigh Uni-sity. There, Oles M. Smolansky, a described "left-of-the-center" Soviet ign policy expert, convinced the Phi a Kappa student that majoring in ign relations wouldn't lead to a life ing cabs. Says Slatkin: "He opened eyes to a whole range of opportuni- in Washington."

ater, at the Georgetown University ool of Foreign Service, she focused defense, though there were few nen in the field. One of her three ɔchildren, 27-year-old country & western singer Kelly Willis, thinks Slatkin breaks into male-dominated worlds "to show it can be done." Slatkin demurs, saying it's "part accident, part sign of the times."

Whatever the case, in Washington her record and her mentors aided her steady ascent. After winning kudos as an analyst at the Congressional Budget Office, she moved to the House Armed Services Committee, where she enhanced her reputation as a procurement specialist. When President Clinton tapped the panel's chairman, the late Les Aspin, to be Defense Secretary, Aspin took Slatkin along. She worked for Deutch, then the Pentagon's acquisitions chief, who in turn pushed her for head of procurement at the Navy, where she oversaw a $26 billion annual acquisition budget. There, her tough questions unsettled the brass and earned her the nickname "Tora Nora."

Noting Slatkin's limited managerial experience, one congressional source lumps her with a group of aides who "wound up in positions not due to the fact that they were superbly competent, but they happened to have a connection to Les Aspin." On the other hand, says the source: "She didn't screw up when opportunity knocked."

Indeed, Deutch was so impressed with her skills—she helped rescue such overbudget programs as the Seawolf submarine—that when he became CIA director, he named her to her current $122,688-a-year job. "She's a tremendously capable person," he says. "You give her a management problem, and it gets resolved."

Now Slatkin is putting in 60-hour weeks and working the mobile phone during early-morning and late-night commutes between her home in Annapolis, Md., and CIA headquarters in Langley, Va. Says a senior Navy official: "She is an absolutely driven person."

So driven that it was perhaps inevitable she would meet her husband at work. Slatkin and Oklahoman Deral E. Willis, a laid-back retired paratrooper who works for Senator Ernest F. Hollings (D-S.C.) on defense and foreign policy, first crossed paths when she was at the CBO and he was the Army's congressional liaison with the office. They married in 1982. These days, they like to spend weekends boating on Chesapeake Bay. But so efficiency-minded is Slatkin that they recently bought a 38-foot diesel trawler instead of a sailboat—to avoid wasting time drifting.

UNPRECEDENTED. Slatkin doesn't want the CIA to drift, either. She is requiring unprecedented five-year budget plans from each of the four directorates: Intelligence, Operations, Science & Technology, and Administration. And she asks hard questions about them, especially if a plan doesn't support the agency's focus on such areas as terrorism and narcotics. Says Gannon: "She is quite capable of stopping a briefing when she thinks inadequate preparation has been made."

Slatkin's biggest challenge may lie in revamping the agency's balkanized personnel system. The Intelligence unit alone has 10 geographic offices that jealously guard their control over personnel slots. Conducting intelligence in Bosnia involves coordinating six offices.

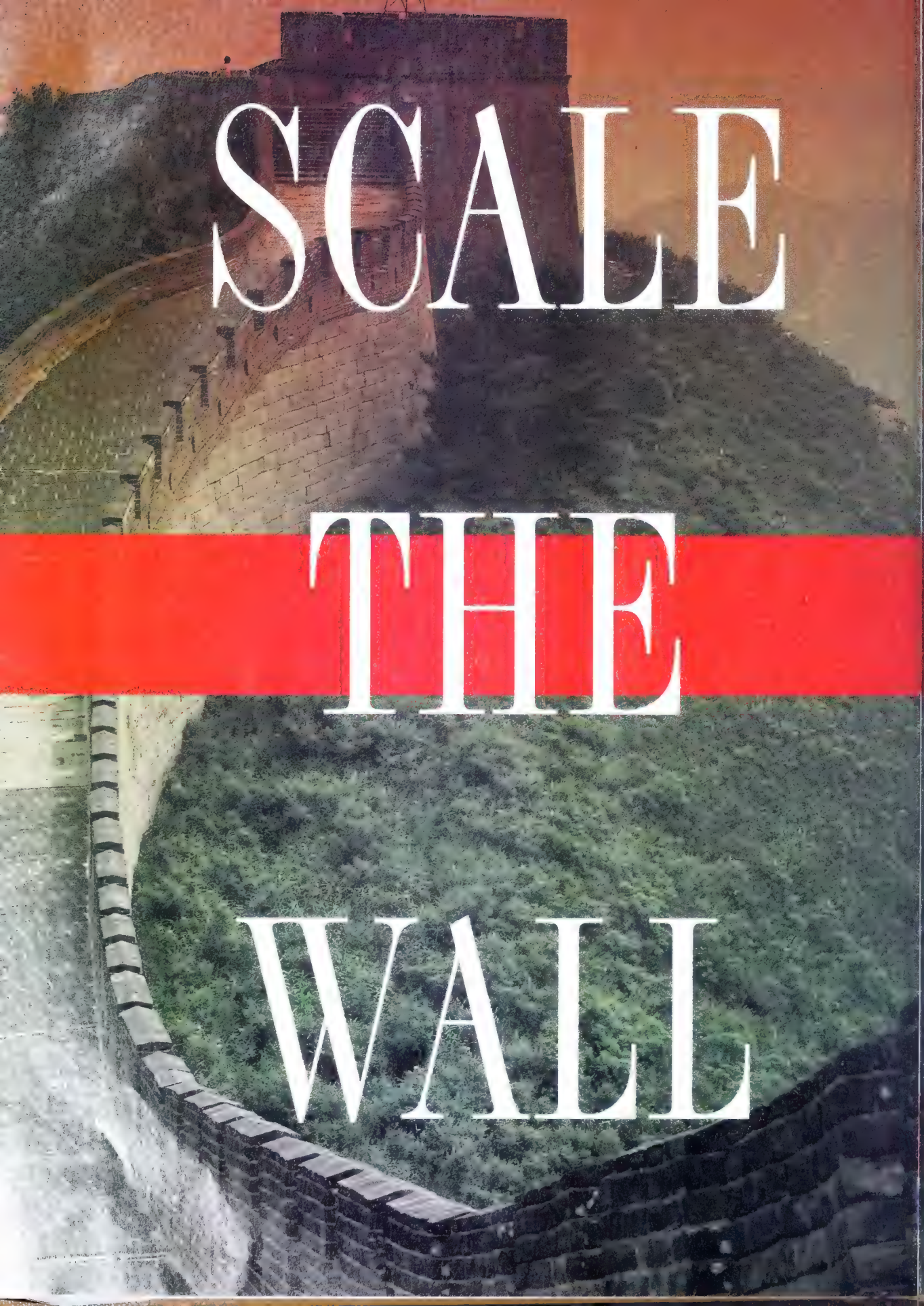
Slatkin says she also wants to "have fair practices" and make sure people are rewarded for performance. Even routine personnel decisions at the CIA have a Kafkaesque quality. Filings in the sex-discrimination suit alleged that "'secret files' that are never seen by the victims" often scotched promotions. Sources say officials cite national security to hide the reasons for some decisions.

Slatkin has set up a Human Resources Oversight Council to consolidate personnel management, and recruiting is now centralized. But she's pressing top officials to move faster. This spring, she will unveil an agencywide career-development program that will offer employees more training. "We want to recruit, attract, retain, and develop the very best people in America," she says.

That's a tall order. And the odds may be stacked against her. Budgets are tight, the CIA's reputation is bruised, and its galvanizing force, the Evil Empire, is gone. Slatkin is confident about her game plan. But even with Deutch squarely behind her, she'll need all the spine she showed on Capitol Hill.

By Stan Crock in Langley, Va.

kin concedes. "It doesn't mean I can't do this job."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EDITED BY AMY DUNKIN

HOSPITALS: CHOOSING WELL TO GET WELL

Sunshine filtering through a skylight bathes the lounge as the pianist plays an old favorite. People congregate in small groups or sidle up to a buffet cart loaded with fruits and pastries. It could be any Marriott at teatime, except that many of the guests are wearing pajamas and some are in wheelchairs or hooked to intravenous drips. They're patients of Columbia-Presbyterian Medical Center's McKeen Pavilion, a hospital floor in New York with the amenities and ambiance of a hotel. Managed care? On this floor—where rooms cost $250 more than the regular $1,290 per day—care goes to those who can manage to pay.

Facilities such as McKeen point up a dichotomy in American health care. Managed care has compelled hospitals to cut staff, shorten inpatient stays, and shift treatment to ambulatory settings. Yet competition has also forced them to find new ways to cater to the needs of patients, especially those who have discretion over where they go for treatment. "You are seeing two pictures," says Dr. Arthur Kaufman, a physician who evaluates medical practice at Veterans Administration hospitals. "One is focusing on individuals and their satisfaction with the hospital environment. The other is getting them to come in and get out fast."

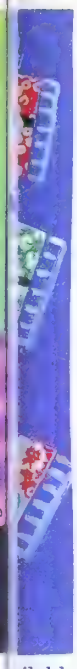
PREVENTION. Given this reality, the big question is how to get access to the best hospital care possible. Few people are completely unrestrained in their choice. Where they receive treatment will be limited by the parameters of their health plan and ability to pay. But even in this age of managed care, people should evaluate their options. Once they do, some patients, in reverse of customary practice, actually select a hospital first, then sign up with an affiliated doctor. "Whatever you do, don't wait until you are sick to investigate because that's when you are vulnerable and anxious," says Geraldine Dallek, director of health policies at Families USA, a Washington (D.C.) consumer group.

BENEFITS

Traditional fee-for-service health insurance offers the greatest freedom to choose. A typical plan pays 80% of hospital costs after a deductible of about $500 per person, and 100% after the patient has spent $1,500 out of pocket in a year. Although the hospital you select ceases to be an issue, fee-for-service patients cannot just check themselves in at will. Many procedures and tests require clearance from the health plan's utilization manager first. And it's importan make sure that hosp charges fall within the in er's guidelines for reason costs. Otherwise, the ho tal might bill you for c the health plan won't cov

If you belong to a hea maintenance organizat your choice will be restri to hospitals under cont with the HMO. The plan usually pay 90% to 100% all costs for an approved cility. If you have the op to leave the network, y generally be reimbursed 70% of the costs, and a ductible of several hund dollars may apply.

ENOUGH NURSES? In pic a hospital, whether fro preapproved list or not, sure to check out doctor ommendations, hospital utation, and published on medical outcomes, de rates, numbers of board tified staff, and the rati registered nurses to b



You'll find these in the *Consumer's Guide to Hospitals* ($12, Center for the Study of Services, 800 213-7283) and *America's Best Hospitals* ($19.95, John Wiley & Sons). You can also contact the Joint Commission on Accreditation of Healthcare Organizations (708 916-5800), which makes the results of performance reports ilable for $30 apiece.

If you don't already have a orite primary physician, ittle down the list of net-rk providers with an eye vard their admitting privi-es at specific hospitals. ep in mind that most doc-s will refer you to special-s at the same hospital they nit you to, notes Robert ughoff, president of the nter for the Study of Ser-es, a Washington (D.C.) nsumer group. To avoid iting your options, try for physician who has admit-g privileges at more than e place. One could be a ge medical center that pro-es acute care and is well ipped for complicated ill-sses, such as cardiovascular ease. The other could be community hospital that's able of treating less risky esses and is situated clos-to home.

Find out if your health n requires that you use e of its designated "centers excellence" for unusual or nplex cases, such as trans-nts or cancer therapy. The nters are usually teaching spitals affiliated with ma- medical schools, and many alth plans will pay travel penses for the patient and family member. Treatment such a hospital often pro-vides access to the highest levels of medical knowledge. But it also means you will be examined by teams of medical students or residents, and that a significant portion of your care could be delegated to these trainees. That's a major drawback for some people, warns John J. Connolly, editor of *How to Find the Best Doctors, Hospitals and HMOs for You and Your Family* ($9.95, Castle, Connolly Medical).

DON'T BACK DOWN. If you want to receive coverage from a hospital that's outside of your plan, you must make a convincing medical case that you will benefit. For this purpose, it helps greatly to have a primary doctor who will go to bat for you. Also be prepared to wage a letter-writing campaign to the health plan as well as the hospital. Sometimes you can get the facility to cut a deal under which it will accept what your insurer normally pays. You have a better chance of getting your plan to be flexible if you're not going to cost it more money.

To get an idea in advance of how customer-conscious a hospital is, walk in the front door and see how well you are treated. Call the hospital to see if it makes customer-satisfaction surveys available. Then try to find people you know who were treated for the same types of illnesses. Were calls for assistance answered promptly? Are patients lost in the shuffle? Were the nurses caring and supportive?

Many hospitals have comfortable private rooms for an extra charge of $100 or more. At Columbia-Presbyterian's McKeen Pavilion, a concierge is on hand to assist with errands, and the dinner menu includes such items as roast salmon in a porcini crust. Tea is served daily at 3 p.m. in the glass-enclosed lounge. Health plans refuse to pay for private rooms unless there is a medical reason, but Columbia-Presbyterian finds patients who are willing to dig deep for the added comfort of McKeen. Catharine Kelly, 70, who suffers from cardiovascular disease, recently returned to McKeen for treatment of a serious foot infection. She says the care and comfort speeds her recovery—and for that reason "the best, in the long run, is the least expensive."

State teaching hospitals have less costly private and upgraded rooms. For example, the University of Illinois at Chicago Medical Center has a carpeted, wallpapered VIP suite in a quiet corner of most of its floors, says Sidney Mitchell, executive director. It costs $120 above the hospital's regular daily private-room rate. At the Medical University of South Carolina in Charleston, the 42-bed Palmetto Pavilion has wood-trimmed walls and early American furnishings. A room costs $450 a day, the same as the other rooms in the hospital, which are all private. A two-room suite costs an extra $50.

HEALING PETS. Instead of seeking luxury, you may want a hospital that focuses on your emotional health. St. Luke's Episcopal Hospital in Houston encourages patients to take up art as part of a program to provide a healing environment. For people who need cheering up, it arranges visits with dogs and rabbits. Such special support services have helped David Atchley, a 52-year-old oil refinery maintenance manager, through the ordeal of waiting since last July for a donated heart.

Very few healthy people like to dwell on the possibility that they may need hospital care one day. But evaluating choices ahead of time can make a huge difference. You may get the kind of treatment that leaves you feeling more like a respected guest—and less like a helpless inmate. *Richard Korman*

Some patients say they select the hospital first, then sign up with an affiliated doctor

ISSUES THAT SHAPE HOSPITAL CHOICE

YOUR PRIMARY-CARE DOCTOR You want a physician with admitting privileges at desirable hospitals. You also want someone who will make the case with your insurer or managed-care provider to send you to any hospital that is medically best for you.

MEDICAL CARE Don't rely just on reputation and a doctor's recommendations. Seek data from accrediting bodies and surveys that provide statistics on medical outcomes, numbers of board-certified staff, and other measures. Discount experiences of acquaintances who have been in the hospital unless they were treated in the same department.

NURSING STAFF This more than any other factor affects the quality of your stay day-to-day. Nurse-to-patient ratios have been declining, but try for better than one to ten.

AMENITIES You should find clean, comfortable rooms; nutritious food that is appetizing; flexible visiting hours; and extra services such as massage therapy or access to office machines.

DATA BUSINESS WEEK

THIS MARKET COULD KEEP COOKING WITH GAS

Natural gas prices are hot. The most closely watched spot-market price, the Henry Hub, was $3.60 per thousand cubic feet in January. Compare that with December's average of $2.31, or January 1995's average of $1.61. "No one expected gas prices to go through the roof like they have," says Michael Smolinski, First Albany's gas analyst. Why? Experts think the industry was unprepared for this season's colder-than-normal temperatures after five years of mild winters—including that of 1995, one of the warmest on record.

SMART MONEY

But why jump into these stocks just as gas prices begin to ease off their seasonal highs? In 1989 and 1993, prices spiked, and everyone was calling a market turn. But this time, many industry watchers are predicting prices to be higher than expected, at least for the next six months. Precariously low gas-storage levels, Canadian pipeline constraints, and strong electric and industrial demand could put pressure on gas supplies through the year, buoying prices and leading to gains for producers.

NATURAL HIGH? What's more, "these companies have strong fundamentals and are relatively cheap," says Richard Weiss, the value-seeking manager of Strong Opportunity and Common Stock funds. This sector is trading at the low end of its historical range—7 times cash flow. "They are still 15% to 20% below their previous cyclical peak cash-flow multiple, which was 9 in 1993," notes Curt Launer of Donaldson, Lufkin & Jenrette. Like shares of many other industries, natural gas stocks have been carried up with the market and are trading near their 52-week highs. But the group's average return was less than half the 34% (not including dividends) of the Standard & Poor's 500-stock index in 1995, which means they may have room to grow.

Low gas inventory levels for the next six months could work in the industry's favor.

Expecting another warm winter, utilities filled gas storage to only 93% of capacity, the lowest level in 20 years. Northeastern and Midwestern cold snaps strained these already-low stockpiles and reduced them 25% under last year's level. With some winter left and the need to refill storage this spring and summer, gas prices could remain strong.

Canadian pipeline constraints may also help to keep prices up. Canadian imports, which have grown 12% per year since 1990, have slowed because of limited capacity. So supplies may be squeezed until the Northern Border Pipeline is completed in mid-1998.

Strong demand is another factor when it comes to supply problems. Electric utilities are using more gas to meet rising electricity needs. The load for electric power has grown 46% in the last 20 years, which in turn has begun to test the industry's capacity limits, notes Smolinski. The ability to turn coal, hydro, and nuclear power into electricity has been limited because new capacity has not been ordered since the 1970s. Last August, electric utilities generated 44.3 billion kilowatt hours using gas—that's the highest rate in 20 years and nearly 20% more than the previous year. "As load continues to grow, capacity limits will begin to show up in off-peak months, too," argues Smolinski.

Investors should focus on companies with heavy gas [illegible] posure, low-cost product[illegible] and development, and h[illegible] reserve replacement rate[illegible] the rate at which a compa[illegible] replaces the oil and gas[illegible] produces, says S. G. W[illegible] burg's Paul Buongiorno. [illegible] ron Oil & Gas is a pure p[illegible] on natural gas, which con[illegible] tutes over 85% of its to[illegible] reserves. Anadarko Petro[illegible] um has about 60% of its [illegible] serves in natural gas, and[illegible] boasts a high 250% repla[illegible] ment rate.

Much of Noble Affiliat[illegible] 60% natural gas reserve b[illegible] is concentrated in the high[illegible] priced area of the Gulf[illegible] Mexico. That's good ne[illegible] says Benjamin Rice of Bro[illegible] Brothers Harriman. So[illegible] gas-producing regions ha[illegible] had lower prices because[illegible] weak regional demand a[illegible] transport problems.

ENERGETIC PLAYS. A f[illegible] small companies, includ[illegible] Cairn Energy USA a[illegible] Chesapeake Ener[illegible] have higher risk b[illegible] may have greater [illegible] ward should natural g[illegible] prices remain stro[illegible] Cairn and Chesapeake ha[illegible] more than 80% of total [illegible] serves in natural gas. Th[illegible] aggressive-growth compan[illegible] are high-volume produce[illegible] depleting wells in three [illegible] five years, compared with [illegible] industry average of eight [illegible] ten. Chesapeake uses [illegible] vanced horizontal drilli[illegible] which reduces the compar[illegible] production costs to 15¢ [illegible] thousand cubic feet, well [illegible] low the 60¢ industry avera[illegible] says Buongiorno.

Still, as with any comm[illegible] ity-based shares, proce[illegible] with caution. A possi[illegible] oil-price drop, should I[illegible] move back into the m[illegible] ket, could depress g[illegible] prices in some regions. [illegible] creased gas supplies a[illegible] result of improved te[illegible] nology and exploration[illegible] a cool summer could a[illegible] squelch these stocks. I[illegible] if the industry bulls [illegible] right and gas prices ho[illegible] these companies will s[illegible] fired up. *Toddi Gut[illegible]*

Hot Stuff

COMPANY	STOCK PRICE (2/12/96)	PRICE TO CASH FLOW*
ANADARKO PETROLEUM	$52⅛	14.4
BARRETT RESOURCES	24⅛	6.9
CAIRN ENERGY USA	13¼	6.3
CHESAPEAKE ENERGY	42⅛	9.6
ENRON OIL & GAS	26⅛	8.9
NOBLE AFFILIATES	31⅛	5.7

* Historical range for the industry is 6 to 16

DATA: S.G. WARBURG & CO., FIRST ALBANY CORP., BLOOMBERG FINANCIAL MARKETS

ELCOME TO THE WORLD IDE ART GALLERY

ONLINE

ıen Stewart ltzer, an art collector in New York, ;ided to bid on a isse drawing he liked, knew it was within his e range. But before he ponded to the dealer's te, he did his homework g ArtNet, an online data-e. The service let him up photos of similar ks and review their s histories. What he ıd was that comparable vings had sold for around 000 at auction within the t two to three years, ıt 25% less than the dealer asking price for the Ma-e. That information ped Waltzer save more ı $30,000 on his purchase. iewing art online doesn't ace the pleasure of pausing over a work before buying it. Nevertheless, collectors are finding satisfying s to explore the market ıout budging from their What's more, art lovers would rather look than can peruse world-class ections through thousands ıuseum and gallery sites the World Wide Web. ıeral services, such as ıpuServe, America Online, Prodigy, offer much more ted forums for buying and ing art, but they're fine browsing.

TUAL BIDDING. ArtNet 4-ARTNET) is the most ensive of the private on-databases catering to the market. With its special ware, you can get access auction results from 500 ses in 28 countries and 50 international galleries. wever, at a sliding-scale that starts at $1.75 per ute after one free hour a ıth, ArtNet isn't for the ual browser but for the serious collector interested in comparing prices or tracking down select pieces throughout the world.

The major auction houses, Sotheby's and Christie's, both sponsor Web sites that let you view a selection of works for sale as well as order catalogs. Of the two, the Sotheby's offering is the more comprehensive. For example, it provides an interactive crash course on buying art at auction for the uninitiated. Three scenarios walk you through the process, from evaluating the condition of a work to bidding. If your virtual bid doesn't land the item you want during the practice session, a message flashes "Our Condolences."

Popular online services offer bulletin boards for buying and exchanging information about art. The works featured may include everything from comic books to mass-market prints. To avoid getting taken, never purchase anything based solely on the online representation. Either arrange to see the work in person or obtain a money-back guarantee in case you hate it once it arrives.

If you're just interested in browsing, your computer gives you entry to the virtual corridors of some of the world's top museums and galleries. One of the easiest ways to search is through the art section of the Web's Yahoo! directory, which will connect you to a bewildering array of choices. World Wide Art Resources is another excellent passageway, letting users scan more than 7,000 listings. It's a great reference if you're planning to visit a city and want to check out current museum exhibitions. ARTscope is a link away from many major New York and West Coast galleries. And artnetweb allows you to sample the avant-garde of online art, such as the Art Crimes Front Page, which is devoted to graffiti.

SKETCHY IMAGES. Specific museum and gallery online offerings vary widely. The Guggenheim Museum's Web page allows you to view works from its current exhibition, followed by a statement from the artist and quotes from critics. You can also click on the artist's photograph or check out museum schedules. At the Metropolitan Museum of Art site, you will find interactive floor plans that help you wander at will through more than 30 centuries of art. The WebMuseum serves up an array of art sites from Seoul to Berlin that can be accessed through hot links, or words you click on.

Be forewarned: Viewing art online does not offer the clarity of a TV image, much less the real thing. The picture on your screen may appear sketchy, as the widely used 8-bit computer monitors can pick up only 256 colors, compared with 16 million on a 24-bit monitor. A frequent complaint is that it can take an eternity to download images, but this is improving as Web sites are enhanced. On a road test with three online services and a 14.4 modem, it took 2 to 8 minutes to download Edgar Degas' *Dance Class at the Opera* from the WebMuseum. But that's still quicker than going to a library to look up the painting, or, for that matter, flying to Paris to see it firsthand. *Louise Nameth*

ART ADDRESSES ON THE WEB

AUCTION HOUSES

Christie's: http://www.christies.com
Sotheby's: http://www.sothebys.com

MUSEUMS

Guggenheim Museum:
http://guggenheim.lehman.cuny.edu/gugg
Metropolitan Museum of Art:
http://www.metmuseum.org
WebMuseum: http://www.emf.net/wm

SEARCH TOOLS

artnetweb: http://artnetweb.com
ARTscope: http://www.artscope.com
World Wide Art Resources:
http://www.concourse.com/wwar/default.html
Yahoo!: http://www.yahoo.com

DATA BUSINESS WEEK

ILLUSTRATION BY MARGARET FISHER; MONA LISA PHOTOGRAPH BY STEVE LEONARD/THE STOCK MARKET

1996 The Second Annual NII Awards
CALL FOR ENTRIES

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CYBERSPACE

EXCELLENCE RECOGNIZED

The National Information Infrastructure (NII) Awards recognize best practices and excellence in use of the "Information Highway."

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- Community
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- Health
- GII Next Generation

SPECIAL AWARDS

- AT&T NII Telecollaboration Award
- US Postal Service NII Public Access Award
- NII Children's Award

DEADLINES

All entries must be received by May 1, 1996. Enter early - by March 13 - and you will be eligible for valuable prize drawings.

WINNERS

Winners will be honored at a special ceremony in the Fall of 1996 and will be featured in a national education and awareness program.

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FOR ENTRY INFORMATION

Visit **http://www.gii-awards.com** send email to **info@gii-awards.com** or call 800-250-2858

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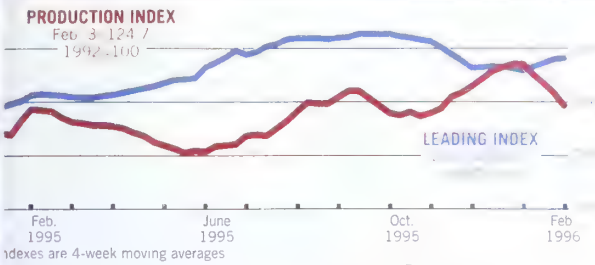
Business Week Index

RODUCTION AND LEADING INDEXES

hange from last week 1.0%
hange from last year: –1.0%

Change from last year: 2.7%



ndexes are 4-week moving averages

production index dropped during the week ended Feb. 3. Before culation of the four-week moving average, the index also fell, to 123.3, n 124.5. Declining auto and truck output led the drop. For the month of uary, the index stood at 125.4, down from 128.6 in December

leading index was little changed in the latest week. The unaveraged index ed up to 257.5, from 257.2. The January index increased to 258, from 5.4 in December.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (2/10) thous. of net tons	1,971	2,030#	0.2
AUTOS (2/10) units	129,830	122,352r#	–10.5
TRUCKS (2/10) units	120,870	108,372r#	2.1
ELECTRIC POWER (2/10) millions of kilowatt-hrs.	68,315	67,886#	4.6
CRUDE-OIL REFINING (2/10) thous. of bbl./day	13,614	13,636#	1.5
COAL (2/3) thous. of net tons	17,722#	20,002	–17.2
PAPERBOARD (2/3) thous. of tons	NA#	NA	NA
PAPER (2/3) thous. of tons	NA#	NA	NA
LUMBER (2/3) millions of ft.	392.4#	449.0	–13.2
RAIL FREIGHT (2/3) billions of ton-miles	22.4#	24.4	–11.5

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA[1], SFPA[2], Association of American Railroads

EADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
OCK PRICES (2/9) S&P 500	650.03	632.94	35.1
RPORATE BOND YIELD, Aaa (2/9)	6.87%	6.82%	–17.0
DUSTRIAL MATERIALS PRICES (2/9)	109.8	109.8	–2.7
SINESS FAILURES (2/2)	NA	NA	NA
AL ESTATE LOANS (1/31) billions	$506.5	$505.8	8.7
NEY SUPPLY, M2 (1/29) billions	$3,644.0	$3,649.3r	1.6
TIAL CLAIMS, UNEMPLOYMENT (1/27) thous.	389	412r	21.6

urces: Center for International Business Cycle Research (CIBCR), Standard & r's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures arge companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on iness failures and real estate loans

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (2/14) $/troy oz.	403.100	414.200	7.2
STEEL SCRAP (2/13) #1 heavy, $/ton	144.50	144.50	0.3
COPPER (2/10) ¢/lb.	121.1	121.1	–11.4
ALUMINUM (2/10) ¢/lb.	75.0	73.5	–21.5
COTTON (2/10) strict low middling 1-1/16 in., ¢/lb.	82.00	83.72	–6.7
OIL (2/13) $/bbl.	18.91	17.69	2.7

Sources: London Wednesday final setting, Chicag[illegible] *Week*, Memphis

TEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
DERAL FUNDS (2/13)	4.93%	5.1[illegible]	5.93%
MMERCIAL PAPER (2/14) 3-month	5.13	5.16	6.16
RTIFICATES OF DEPOSIT (2/14) 3-month	5.13	5.16	6.17
ED MORTGAGE (2/9) 30-year	7.29	7.31	9.04
JUSTABLE MORTGAGE (2/9) one-year	5.39	5.49	6.73
IME (2/14)	8.25	8.25	9.00

urces: Federal Reserve, HSH Associates, Reuters Holdings PLC

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (2/14)	106.81	106.03	97.30
GERMAN MARK (2/14)	1.47	1.48	1.48
BRITISH POUND (2/14)	1.54	1.54	1.58
FRENCH FRANC (2/14)	5.06	5.08	5.16
ITALIAN LIRA (2/14)	1580.5	1576.2	1607.3
CANADIAN DOLLAR (2/14)	1.38	1.37	1.41
MEXICAN PESO (2/14)	7.505	7.460	6.090

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

ew data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense ipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

DING INDICATORS

sday, Feb. 20, 8:30 a.m.EST ▶ The ex of leading indicators, now compiled he Conference Board, was probably flat ecember, after slipping 0.3% in ember. The November index is expected e revised sharply now that more govern- nt data are available. The index has not n since August.

MPHREY-HAWKINS TESTIMONY

sday, Feb. 20, 2 p.m.EST ▶ As required aw, Federal Reserve Chairman Alan enspan will appear before the House committee on monetary policy to testify he conduct of monetary policy and dis- e the Fed's central-tendency forecast for economic growth, unemployment, and inflation for 1996.

FEDERAL BUDGET

Thursday, Feb. 22, 2 p.m.EST ▶ The Treasury Dept. is expected to report a January surplus of $20 billion, according to the median forecast of economists surveyed by MMS International, one of The McGraw-Hill Companies. Washington had a surplus of $15.6 billion in January, 1995.

GROSS DOMESTIC PRODUCT

Friday, Feb. 23, 8:30 a.m.EST ▶ Real GDP probably grew at an annual rate of 1.6% in the fourth quarter, says the median MMS forecast. However, a big improvement in foreign trade may have lifted growth closer to 2% or more. The economy expanded at a 3.2% pace in the third quarter, but domestic demand slowed sharply at yearend. The GDP deflator probably increased at a 2.3% annual rate in the fourth quarter, about the same rise as in the third.

HOUSING STARTS

Friday, Feb. 23, 8:30 a.m.EST ▶ The MMS survey forecasts that housing starts fell sharply to an annual rate of 1.25 million in January, from a likely 1.3 million in December and a 1.42 million rate in November. The East Coast blizzard plus record cold temperatures across much of the nation quashed homebuilding last month.

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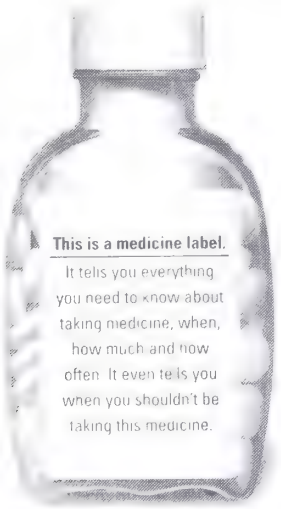
"If direct marketing is part of the mix and technology companies are prospects, I can't imagine a better tool than CorpTech. It is quality information that pinpoints the industry, products and people I need to reach." *Scott Trudo, CaseView Software.*

Need some help identifying your high-tech prospects? Order your 1996 CorpTech Directory today -- now also available on CD-ROM. For **FREE** information package, call 1-800-333-8036.

The Medicine Label... Your Road Map to Good Health



...wouldn't drive across the country without consulting a road map, you should never ... medicine without first reading ... your road map to good health.

A public service from the Council on Family Health

Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

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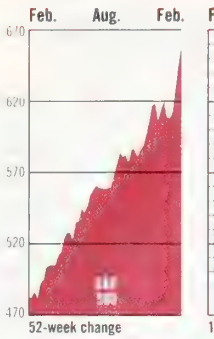
Business Week (ISSN 0007-7135) published weekly, except for one issue in January, by The McGraw-Hill Companies, Inc. Executive, Edit... Circulation, and Advertising Offices: 1221 Avenue of the Americas, New York, N.Y. 10020. U.S. subscriber rate $49.95/year; Canada $69/year. Second-class postage paid at New York, N.Y., and at additional mailing offices. Postage paid at Montreal, P.Q. Canada Post Interna... Publications Mail Product Sales Agreement No. 246484. **Postmaster:** Send address changes to BUSINESS WEEK. P.O. Box 430, Hightstown, NJ 0...

nvestment Figures of the Week

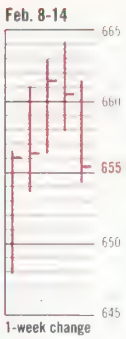
MENTARY

week in the U.S. equity ts. Nasdaq stocks and the ard & Poor's 500-stock in- se to six consecutive all- ighs before falling back on 3. Meanwhile, the Dow industrial average reached highs before falling on Feb. e Feb. 14 decline sent the elow 5600—which it d, for the first time, on 2. Economically sensitive were strong. Bonds rallied eb. 14, when traders be- uncertain about upcoming mic reports.

STOCKS

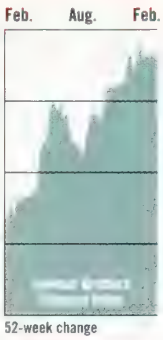


52-week change
+35.3%

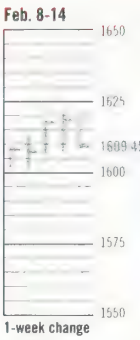


1-week change
+0.9%

BONDS

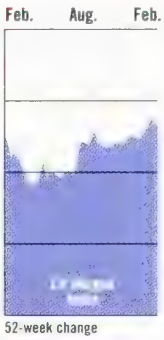


52-week change
+15.5%

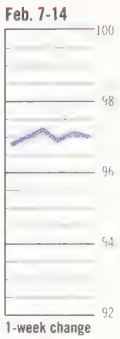


1-week change
+0.2%

THE DOLLAR



52-week change
+0.7%



1-week change
+0.2%

RKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
ONES INDUSTRIALS	5579.6	1.6	40.0
ZE COMPANIES (S&P MidCap Index)	226.5	1.1	26.7
COMPANIES (Russell 2000)	321.1	0.5	24.7
)MPANIES (Russell 3000)	371.8	0.8	33.9

IGN STOCKS	Latest	% change (local currency) Week	52-week
)N (FINANCIAL TIMES 100)	3745.0	0.5	21.8
(NIKKEI INDEX)	20,943.6	0.0	16.4
ITO (TSE COMPOSITE)	5059.7	0.7	22.7

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	4.93%	4.94%	5.88%
30-YEAR TREASURY BOND YIELD	6.09%	6.15%	7.56%
S&P 500 DIVIDEND YIELD	2.10%	2.11%	2.68%
S&P 500 PRICE/EARNINGS RATIO	18.9	18.8	16.2

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	577.9	574.3	Positive
Stocks above 200-day moving average	72.0%	71.0%	Negative
Speculative sentiment: Put/call ratio	0.68	0.63	Neutral
Insider sentiment: Vickers sell/buy ratio	1.66	1.63	Positive

BLOOMBERG FINANCIAL MARKETS

DUSTRY GROUPS

MONTH LEADERS	% change 1-month	12-month	Strongest stock in group	% change 1-month	12-month	Price
. AND GAS DRILLING	24.2	65.8	ROWAN	24.3	95.7	11 1/2
MMUNICATIONS EQUIPMENT	23.2	67.2	ANDREW	44.5	28.0	49 1/2
TELS AND MOTELS	22.3	30.3	HILTON HOTELS	31.7	27.6	88 3/8
RSONAL LOANS	22.1	51.5	HOUSEHOLD INTERNATIONAL	26.3	67.8	67 3/4
MPUTER SYSTEMS	19.6	44.9	DATA GENERAL	42.9	105.9	17 1/2

MONTH LAGGARDS	% change 1-month	12-month	Weakest stock in group	% change 1-month	12-month	Price
CHINE TOOLS	–2.1	0.2	CINCINNATI MILACRON	–2.5	6.0	24 1/4
LLUTION CONTROL	–1.2	5.5	BROWNING-FERRIS INDUSTRIES	–3.3	–8.6	29 1/8
MEBUILDING	0.6	22.2	CENTEX	–6.1	11.1	28 1/4
NERAL MERCHANDISE CHAINS	1.2	4.2	WAL-MART STORES	–1.1	–7.4	22
OES	2.2	38.7	BROWN GROUP	–7.2	–61.0	12 7/8

UTUAL FUNDS

MORNINGSTAR INC.

ERS

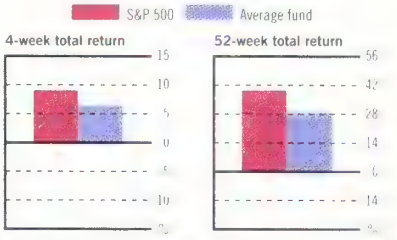
week total return	%
INITREND GOLD	18.2
HG SELECT EQUITY	18.1
EYFUS AGGRESSIVE GROWTH	18.1

eek total return	%
DAS	94.6
DELITY SELECT ELECTRONICS	76.1
GER CAPITAL APPRECIATION	76.0

LAGGARDS

Four-week total return	%
GRANDVIEW RETAIL REALTY INCOME	–5.2
WRIGHT EQUIFUND-SWITZERLAND	–3.7
CRABBE HUSON SPECIAL	–2.6

52-week total return	%
EV MARATHON GREATER INDIA	–24.4
AMERICAN HERITAGE	–24.1
STEADMAN TECHNOLOGY GROWTH	–22.0



LATIVE PORTFOLIOS

DRI/McGRAW HILL

r amounts represent the ent value of $10,000 ted one year ago ch portfolio

entages indicate day total returns

U.S. stocks	Treasury bonds	Foreign stocks	Money market fund	Gold
$13,967	**$12,975**	**$12,192**	**$10,562**	**$10,236**
+2.19%	+0.69%	–0.41%	+0.12%	–2.73%

ta on this page are as of market close Wednesday, Feb. 14, 1996, unless otherwise in- d. Industry groups include S&P 500 companies only; performance and share prices are as of market close Feb. 13. Mutual fund returns are as of Feb. 9. Relative portfolios are val- ued as of Feb. 13. A more detailed explanation of this page is available on request. r=revised

WHAT DOES THE GOP REALLY WANT?

Forgive us for being a little confused. The GOP took Washington by storm in 1994 on a platform of balancing the budget. Budget reduction was written into stone: the Contract With America. There was talk of a constitutional amendment mandating the elimination of government deficits. And now? Nary a whisper about deficit reduction among Republican primary candidates.

Instead, there are new voices. Steve Forbes sings about tax cuts that will suddenly double economic-growth rates. So much growth, we are told, that we won't have to really cut government spending deeply. No pain, all gain. Pat Buchanan shouts darkly about enemies in Big Business, immigrants stealing jobs, and the need for protectionism. In a world of the global Internet, he prescribes tariffs. Will the real GOP economic platform please stand up?

We think reasonable people agree that economic policy should revolve around the twin tasks of cutting the deficit and promoting growth. The two are intertwined. Balancing the budget would curb government borrowing and send interest rates down. That, in turn, should set off a refinancing surge, putting cash into consumers' pockets. Lower rates should also prompt a capital-investment boom, boosting profits and jobs.

Then cut marginal tax rates to allow individuals and corporations to keep more of what they earn. The flat tax would, in all probability, increase, not decrease, the budget deficit. True believers in the Republican party say that a 17% flat tax will generate enough economic growth and tax revenue to balance the federal budget without the pain of spending cuts. I wish with all our hearts that it were true. But little in lif gained without discipline and difficulty, and we suspect t curbing entitlement spending is one of them.

Balancing the budget must be done through real fi sacrifice, not economic alchemy. Spending cuts accompanie tax cuts can be a potent policy brew that moves the econ to a new, higher plateau of growth, say 3% to 3½% per y At that rate, politicians in Washington might eventually e have a bit of a budget surplus to squabble over.

What is not acceptable is the protectionist demagogu now spreading within the GOP. The Republican Party's hist tradition of free trade and open markets is being tarnished an ugly kind of economic nationalism. Even the mode Senator Bob Dole, to his shame, is beginning to echo the threats of extremism. There is no way to suppress the t revolutions of technological change and market globalizat and there are no enemies to blame. Quite the contrary: G alization and technology can spur growth.

It is time for the GOP to get a grip. Primaries by their ture tend to push candidates to extreme positions as eac them rushes to curry the favor of small, tightly organized ing groups. But the Republican Party is fast splitting into tions proselytizing strange, and dangerous, economic fai The common ground for GOP economic policy revolves aro reducing the budget deficit and cutting taxes responsi The party should return to it as soon as possible.

GOOD FENCES MAKE FOR LOUSY INTRANETS

It is a powerful new information technology than can unlock huge productivity gains. No, not the Internet. It's the intranet—and it's coming your way. Just as the Internet connects people around the world, the intranet links folks within a single corporation. In fact, intranets use much the same software as the Internet to connect computers and people.

The promise of intranets is one of corporate collaboration and synergy. If executed properly, an intranet ties together islands of data within the vast interstices of corporate bureaucracy, sparking new products and productivity. Intranets have worked wonders for companies as diverse as 3M and Federal Express Corp. (page 76).

But a warning to the wise: Intranets work only if operating units within companies allow their data to be shared. Of course, there are minor benefits by simply putting company directories, newsletters, and cafeteria menus on an internal Web site. But the larger impact is lost when units refuse to divulge what they consider proprietary information to colleagues. Sadly, operating units often build higher walls between themselves and competing units within the same company than against outside rivals. When they do "share" information, they often make it difficult to retrieve. To use power of intranets, these barriers to the free flow of infor tion across corporate boundaries must be broken down—that is as much a political decision as a technological one

Ditto for top managers hogging intranets. The eas intranets is tempting some executives to use them to com nicate down rather than across. Endless streams of annou ments about issues peripheral to today's work and tomorr product innovation clog the systems. Worse, they signal the intranet is not a technology to be used collaboratively horizontally, but hierarchically. If corporations are not car intranets can make for excellent command-and-control syst rather than liberating communication channels.

When intranets are designed the right way, they can s work and promote creativity. The DreamWorks SKG triu rate of Steven Spielberg, Jeffrey Katzenberg, and David fen is using an internal Web setup and Netscape browser manage the creation of a company. It may be that intra work best for new companies that have few bureauc walls. But we think they can be mighty effective for es lished companies as well.